ECONOMIC PROBLEMS
OF
MODERN INDIA

EDITED BY
RADHAKAMAL MUKERJEE
AND
H. L. DEY

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A PREFACE TO PLANNING

By Radhakamal Mukerjee

Movement Towards Planned Economy.—Economic planning has assumed significance throughout the world with the end of *laissez-faire*. As economic nationalism has become stronger and more thorough-going, economic planning has become more pervasive, embracing agriculture, industry, trade and finance. Before the Great War economic planning was more or less social engineering, focusing its attention chiefly to the problems of regulation of conditions of labour, housing, relief of unemployment and social welfare in general. In the post-war economic world, planning has become true of every important sector of economic life. In a socialistic country like Russia the State has now become not merely a comprehensive social welfare agency but also a vast business organisation. The Fascist countries also exhibit a completely controlled economy, but for reasons different from those which underlie Soviet economic planning. In Germany, and in a less extreme form in Italy, foreign exchange, foreign trade, wages and prices are all completely regulated by the State for the sake of pushing a programme of economic autarchy and intensive rearmament. But in the so-called democratic countries, where the course of production and employment is still settled by the expectation of private profits, the State not only undertakes social ameliorative programmes but also regulates the movements of commodities and gold and the functions of credit and currency to an extent unknown before. The distinction between socialistic or dictatorship countries and the capitalistic or democratic countries has now become one of degree rather than of kind. It is probable that as the present trade recession develops the democratic countries, where the unfavourable

reactions of depression will be experienced much more than in their Fascist rivals, will move further along the road toward State control, and their economic apparatus will tend more and more to become assimilated to that of the totalitarian States. It will be useful to give a brief outline of planned economic policy which will be of immediate significance for India, bearing in mind the schemes and undertakings successfully adopted in the agricultural countries of the West, especially the U.S.A. and Soviet Russia, with which India shows marked resemblance in the general configuration of her economic life.

Agricultural Planning: conservation of soil and water.— India maintains the largest agricultural population on the basis of subsistence farming in small holdings but she hardly realises that much of the soil's fertility, which is her most valuable legacy, fundamental source of her wealth and basis of prosperity, is slipping away from her. Soil erosion is the greatest single menace facing Indian agriculture to-day. In many areas as human and animal population has expanded beyond the limits and resources of the village fields and groves, the axe and the plough invade and appropriate all uncultivated wastes. The destruction of forest or scrub jungle and the extraction of stumps and roots lay bear the ground and exposes it to the quick work of water and wind erosion. Its devastating effects vary according to soil and topography and the intensity of population pressure. With the loss of the top soil and failure to replenish the depleted plant food, when cow-dung, the only available cheap manure is burnt due to the scarcity of fuel, the impoverished soil shows on the whole lesser yields. Recent investigations show that in the bare fallow fields in the foothills of Northern India, except properly levelled rice land, a single storm leads to the loss of soil at the rate of $1\frac{1}{4}$ tons per acre, while in the Bombay Deccan there is a loss of 133 tons of soil per acre per annum from a field of *jowar*. In the face of rapid scouring of the soil, the improvement of crop varieties or introduction of chemicals are more or less a drop in the bucket of

productivity. Such scouring is especially acute in India along the Himalayan foot-hills and sloping ground throughout Northern India, in parts of Madras, the Bombay Deccan, the outer provinces, the Punjab and the Central Provinces, Chota Nagpur and Central India. Besides, along the banks of most of the bigger rivers soil erosion has led to the formation of a vast and intricate network of fissures and gulleys and the loss of invaluable agricultural land. Soil erosion is responsible for 8 million acres of ravine lands in the U.P., for the man-made desert between Rajputana and the United Provinces, which is now invading her south-western districts, and for the partial filling in of reservoirs and choking of irrigation courses in the Punjab and United Provinces. Ravine formation is a serious and increasing menace to agriculture and the village in several parts of the Ganges plain. In one particular district in the United Provinces there are about 12 lakhs of acres of ravine land, and 1,000 acres of good cultivable land are annually lost to cultivation as the result of erosion. In those parts of India where the rainfall is deficient, soil-erosion is also aided by wind-erosion.

It is in the United States that we find the most comprehensive planned combat with erosion. Twenty-two states have passed laws for the creation of soil conservation districts. In India only comparatively small areas of forests are under Government management; forest officers are few, while legislation is also inadequate. Forest conservation and replanting, gulley-plugging, terracing and levelling of fields, and strengthening of field banks by growing fodder crops are the major control measures necessary for dry, badly eroded areas in India. The construction of dams, *bandhs* and embankments, combined with the development of many terraced pits which are built out along the sides of the ravines and on the steeply sloping land, will also be found useful in erosion and gulley control in moist zones. Such measures have been taken in some parts of the Punjab and the U.P., but the work is but a small fraction of what is now necessary. Only one province, *viz.*, the Punjab, has become alive to this menace

and is about to create a special department to deal with soil-erosion. The problem is also bound up with the regulation of excessive and indiscriminate grazing of herds and flocks. The Forest Department should extend its activities along the line of co-operation with the cultivator, who is faced with increasing fodder shortage for his multiplying cattle. It is found in some areas that the cutting of grass for cattle instead of permitting them to graze in it results in a greater yield. Without the co-operation of village *punchayats* in the control of grazing and improvement of natural grasslands, many fertile areas of India would share the fate of the *Brajabhumi*, once flowing with milk and honey, but now stripped entirely of its vegetative covering, a cattle-made desert extending over several hundreds of square miles in the heart of the world's most fertile plain. In the face of the mass movement which has synchronised with the advent of autonomy in the Provinces, there is special danger of preferring the immediate demands of the peasantry for free grazing of cattle and relaxation of forest control to the needs of the generations yet unborn. That danger is aggravated every decade by the quick multiplication of humanity and its cattle, the improvident consumption of their capital assets of soil, trees and grass and the increase of ecologic disbalance of soil, vegetation and water. Such disbalance leads not only to diminishing returns in agriculture but also to an increase of aridity, especially in the zones of precarious rainfall, which makes replanting of forest and grass in any area, denuded by nature, man or cattle, impossible. If the man-made desert between Rajputana and the United Provinces is now protruding its dry, thirsty tongues into the south-western part of the Ganges Valley, man's improvident exploitation of timber, fuel and grass in the Himalayas is a similar crime which brings about devastating recurrent floods and jeopardises the agriculture of the plains from the Punjab to Assam.

Co-ordinated Development of Forestry, Erosion and Flood Control.—Land planning and water planning are interlocked with

each other. Soil washed from the hill slopes, fallow lands and pastures tends to fill reservoirs, clog irrigation courses and stream-channels. Agriculture, irrigation and navigation are all affected. The denudation of the Himalayan slopes, the undue increase of cultivation on the hill-sides and the seasonal concentration of migrant flocks along the travel routes leading to the meadows of the upper ranges have brought about unmeasured losses of soil and water and will be an increasing menace to irrigation and agriculture in the valleys below. In the Punjab soil-erosion has increased the load of silt derived from the Jammu and Gujrat foot-hills which is carried by the Jhelum River, and this has decreased the carrying capacity of the upper Jhelum Canal by 40 per cent, even after the expansive installation of a number of silt ejectors. The increase of the run-off and loss of soil in the less adequately covered hill slopes of the Tehri-Garhwal region will, it may be expected, similarly result in the partial filling in of reservoirs and the clogging of irrigation ditches before long, to say nothing of the difficulty which will be caused by this sediment in operating many of the hydro-electric plants.

In the United States the Tennessee Valley Authority created by the Congress in 1933 is the most interesting regional planning agency for the co-ordinated development of agriculture, forestry, navigation, soil-erosion and flood control. Similar regional authorities, composed of planning boards of different States, have been proposed for various other river valleys. In India irrigation and water problems should no longer be treated as Provincial subjects. In the up-river areas the expansion of agriculture and population involves deforestation, soil-erosion and interference with the river system, which give rise to problems of more than local significance. As population has multiplied and the plough and the axe have ascended the hill-sides, the destruction of forests in the catchment areas of the rivers and their tributaries has caused rapid run-off and erosion leading to the deposit of an increasing mass of debris on river-beds in low lands, thus increasing the damage from floods. The Goghra, the Gandak and the Kosi, the Son

and the Suvarnarekha, the Ajaya, and the Damodar, the Tiesta, the Padma and the Brahmaputra, the Mahanadi and the Godavari—all bring floods which are in large measure due to deforestation in the hills. The increasing severity and frequency of floods in recent years in Bihar, Orissa and Bengal are due to man's invasion of the cradle of streams and trees. Over-grazing by countless flocks of cattle, sheep and goats in the up-river areas also causes much erosion. The evil of the extension of ravine lands is not confined to the United Provinces and the Punjab but extends to the Bengal and Sind Delta where the removal of soils of whole valleys by denudation has led to the silting up of river-beds and the meandering of rivers. The reclamation of swamps in Oudh, the eastern districts of the U.P., Northern Bihar and Assam has also forced an exceedingly heavy run-off. It is estimated that the Ganges now carries to the sea eight times the quantity of silt carried by the Mississippi, and that from a catchment area less than one-third the size. "It is not without significance," reports an irrigation engineer, "that the highest recorded flood in the Ganges occurred in 1924 and that the lowest recorded winter discharge occurred in 1929." There are records of the Ganges for over a century, and the period is long enough to exclude all seasonal cycles. Unplanned canal extension, following the demands of phenomenal population and agricultural expansion in the U.P. and the Punjab, has greatly aided the silting-up process through the diversion of vast volumes of water. Approximately 20,000 cusecs are abstracted from the Ganges and by the Ganges and the Sarda canals, amounting to 30 or 40 per cent of the total discharge of the River Ganges. There has resulted probably a general reduction of summer level of the Ganges by two or three feet which has thereby increased the difficulty of maintaining the connection between the main river and its feeders and channels in the Bengal Delta.

Need of an Inter-Provincial or Federal Development Authority.—Many agricultural and economic problems can be dealt

with adequately only as integral parts of a unified plan for a complete river watershed as a great natural territorial unit. Thus in India we ought to have a Ganges River and an Indus River Commission, a Godavari Board and a Cauvery Board which should arbitrate between the conflicting claims of agriculture and canal irrigation in the up-river areas and navigation and lagoon irrigation in the down-river areas and adopt systematic, co-ordinated measures of afforestation, flood control and river management. Russia has recently completed the Volga canal extension scheme bringing the Volga water to the very doors of Moscow which has been linked with the Caspian Sea, and through other water routes existing or soon to be built with the Baltic, the White, the Azor and the Black Seas. The work of excavation, which was almost twice as much on the Suez Canal, was mainly entrusted with thousands of former criminals and law-breakers who were caught up by the enthusiasm and energy of the great socialist project. Bengal's river-borne traffic is probably the largest in the world, but it still can be enlarged enormously in volume through planned canalisation in Southern and Eastern Bengal, which might remove the congestion of waters in the lower delta and resuscitate the water-ways in the moribund delta. Sind, which is a deficit Province, can enormously increase her wealth through the full utilisation of her water resources by planned canalisation and irrigation development. Planned hydraulic and agricultural reclamation of formerly malaria-stricken marshes has achieved wonders in Fascist Italy. Fourteen per cent of the national territory have been protected or transformed and several new towns and agricultural colonies built to which the surplus population from over-crowded areas is now being diverted. There is a State inland migration and resettlement department for agricultural recolonisation. Malaria and agricultural decay in Northern Bihar, Central and Western Bengal are now spreading like an infection from the dead river zone to the entire river valley. Whether we think of afforestation, erosion-control or hydro-electric development, flood prevention, river management or

re-settlement, the solution lies in each case in the co-ordination of planning under a centralised, inter-provincial or federal development authority.

Crop and Food Planning.—One characteristic feature in Russian and American agricultural planning has been the development of a uniform agricultural practice and organisation in homogeneous agricultural areas growing single, distinctive crops. In India crop planning will have to be undertaken on different lines and correspond to conditions of soil and water supply and to population density. A balanced combination of subsistence farming and industrial cropping should be the aim in the major part of India, where the holdings have become under-sized due to heavy population pressure and where the slump of agricultural prices has now made the cultivation of many crops uneconomical for the small holders. While successful crop planning will depend largely upon an improvement of the yields of rice, wheat and other cereals, subsistence holdings should be encouraged to grow appropriate peas, grams, beans and oil-seeds, which may increase the protein yield per acre and can be more easily assimilated with the particular staple of the peasantry. We often find in India that a cash crop like jute or cane leads to the ultimate exhaustion of the soil and also the impoverishment of the dietary by superseding beans, pulses, oil-seeds and fodder crops. A systematic crop and food planning, taking into consideration the dual need of producing heavy-yielding and energy-producing crops, supplemented as these should be by the accessory food products necessary for health and efficiency, should be undertaken in India, especially in the areas of heavy population pressure. It is in these areas that the holdings are the smallest and food tends to be inadequate or unbalanced; and planned crop production may counteract food deficiency and contribute to improve diet and health conditions and distribute the labour of the peasant families to better advantage throughout the year.

No useful crop planning is, however, possible unless the Indian peasant learns to take a practical view of animal

keeping. It may be estimated that about 125 million cattle out of a total stock of 200 millions are superfluous and uneconomical. In Holland and Germany the State regulates not merely the breeding from pedigree stock but also limits the number of calves which can be maintained in the herds. India must plan deliberately the reduction of her excessive cattle population so as to develop a flourishing export trade of cattle with Africa and the Dutch East Indies and a combination of intensive crop and fodder cultivation with dairying in her small holdings at home.

Planned Marketing and Finance.—That unplanned marketing is the cause of the moneylenders' authority over the peasants' crops, stock and toil is another lesson which can be derived by India from the remarkable methods of improvement of marketing and crop finance in many countries in Europe. One most important mode of rehabilitating co-operation from the effects of the present depression will be to prevent a member of the Co-operative Society from disposing of his produce privately. After voluntary debt conciliation or compulsory liquidation, which will involve wiping out of irrecoverable arrears and quick disposal of saleable fragments of holdings or other assets, such co-operative societies will take over the scaled-down debts of cultivators, place these on a definite long-term basis, and fix reasonable *kists* with the creditors, leaving due margin to enable their debtor members to borrow and repay each year for their seasonal requirements. They will issue promissory notes or warrants in favour of their creditors, endorsed also by the debtors. The security for these promissory notes or warrants should be the crops or dairy produce of the debtor, who must deposit these either in the store-house of the societies or in carts sent to an address indicated by it. The co-operative societies should decide what portion of the crop thus deposited and sold should go towards the payment of instalments to the old creditors. Before each harvest by-laws should be made, as in some agricultural countries in Europe, concerning the procedure in respect of sale of agricultural produce

and payment of instalments to the old creditors. Grading and standardisation of produce, improvement of storage and even the use of granary receipts as bills of exchange will gradually follow, as in the West. Where the existing central banks are operating over small areas, their conversion into effective banking and marketing unions is accordingly the immediate step. Credit activities of the banks and co-operative societies will be strengthened by joint purchase and sale and the entire co-operative movement will be permeated by a new spirit when the co-operative societies are able to assist the peasantry not merely in giving loans but in all the ramifications of the daily routine of agriculture, purchase and marketing and maintain a continuous contact with them. The assimilation of co-operative marketing with rural finance, which is such a striking feature of the agricultural organisation in France and Denmark, and a more effective co-ordination of the financial policies of the Central Banks and the Provincial Bank, will enable the Reserve Bank to give the much-needed relief to agriculture, and help towards the effective integration of co-operative, joint-stock and indigenous banking with the organised banking system in the country.

Rescue of Agriculture and Agriculturists.—During the last two decades agricultural prices continuously rose and rents and revenues had been adjusted to the increased values of agricultural produce by the courts, or by the settlement operations, or by private enhancements of the landlords themselves. Now the pendulum has swung in the opposite direction. The State, the landlord and the money-lender should now all co-operate in preventing an utter collapse of agriculture due to loss of the peasant's credit, and this justifies emergency legislation such as the revision of rents or even partial suspension of the collection of rent and revenue, reduction of the period of land settlement, scaling down of debts, limitation of the money-lender's rates of interest, restriction of sub-letting, mortgage and sale of land and limitation of the expenditure on social ceremonies, as, for instance, recently effected by the Indore Durbar.

The currency and fiscal policies of the last decade increased the real burden of the agricultural classes in India materially. On account of protective and revenue tariff, manufactures have gained, but the gains to agriculture have not been proportionate.

The rationalisation of tenure, rent and revenue policy, the management of agricultural credit and prices, State aid to the movements of agricultural produce abroad by means of imperial or bilateral trade agreements, liquidation of illiteracy, agricultural education and demonstration, State expenditure on works of rural public utility, such as the construction of tramways and light railways, the installation of tube-wells and windmills or the hydro-electric grid system in the country-side for the benefit of agriculture, irrigation and village industries—all these represent the chief features of Provincial developmental policies which have emerged with Provincial autonomy. Rightly conceived and directed these may contribute to bridge in some measure the present gulf between the level of mechanical and economic efficiency in rural and in urban India, and between India's standard of small peasant farming and the level of her competitors in world trade.

Rural Industrialisation.—In India we are now passing through an economic phase in which there are excessive ruralisation and deindustrialisation, as in Bengal and Madras, or there are excessive urbanisation and decline of the village. True economic planning will industrialise the village and ruralise the city so that culture and civilisation may no longer be confined to a few industrial centres but are brought home at every focal point in the rural areas wherever the basis for an industrial life can be found. It will thus develop a variegated type of economic life in the different natural regions of India, mitigate the increasing over-crowding in agriculture, which aggravates poverty, unemployment and diminishing returns in a vicious circle, and establish a state of economic balance in each Province by a judicious combination of cereal and industrial cropping, and the

regional distribution of agricultural, light and heavy industries with reference to the available supply of raw materials, power, labour and the local market. In any integrated economic planning the important *rôle* of such agricultural industries as the production of sugar, vegetable oils and fats, soap, paint and lubricant, and tobacco, leather, paper and hemp factories, which employ the surplus labour on the land and offer facilities to cultivators to obtain remunerative prices for raw materials and industrial crops that may supplement subsistence cropping accordingly, can hardly be exaggerated. Agricultural countries in Europe have such close connection between agriculture and industry that it is at times difficult to draw the line between the spheres of the two. Industry helps in the handling of the produce, supplies the farm with fertilisers, feeding stuffs, machinery and many other subsidiaries and materials. On the other hand, agriculture supplies industry with some of its raw materials. Dairies and milk condensation and powder factories, factories for the preparation of organic therapeutic products, the edible oil industry, milling, canning, chocolate and tobacco industries are all an outcome of the correlation between agriculture and industry in Europe, which has been long overdue in India. Establishment of the basic and key industries; correction of the present uneven character of the industrial system by rural industrialisation; decentralisation of some of the large-scale industries and their transference to regions where these might obtain raw materials and an abundant supply of labour on the spot; and change in the relationship of the industrial centres to one another should be in the forefront of industrial planning.

When industries were granted protection in the past, the entire country was considered as one whole market without an adequate consideration of the larger burden in the case of consumers of those regions which are at a distance from the centres of industrial production. Industries, like labour, tend to be stay-at-home in India and a stress of the cumulative technical, banking and other advantages in a

few industrial centres would divide the country between highly industrialised Provinces and those which will persist as hewers of wood and drawers of water. Such division proceeding on the basis of ear-marking a selected industry for a particular Province and the assistance by tariff and the help of all other Provinces in the disposal of products and getting other facilities may be unconsciously favoured by the special interests of Indian industrial and financial capitalism which now apparently wields great political influence. If the cotton-mill industry of Western India demands sacrifices from the whole country through protected high prices, it cannot remain wholly indifferent to the depression of the coal-mining industry in Bihar and Bengal, whose coal it is now eschewing by its preference of South African coal; while the hand-loom weavers distributed in all Provinces and States represent an important interest which may reasonably demand assistance by adjustment in tariff and by excise. In a democratic federal State like India the experiment towards federalism may itself be jeopardised in the absence of co-ordination between agriculture and industry and of a right balancing of the interests of different regions, while it can be strengthened by a mutual utilisation of products of different Provinces and groups of producers and by the co-ordination of their divergent lines of economic development in a common economic policy.

Quicker Industrialisation of Immature Regions.—Nothing is more characteristic of Russian economic life to-day than the development of thriving industrial centres in the heart of agricultural regions where formerly there were only small industries chiefly engaged in the manufacture of agricultural necessities. The economic transformation of agricultural regions which formerly produced exclusively cereals and sub-tropical raw materials and were more or less semi-colonial dependencies of Russian Czarism has rested on three programmes: (1) the development of hydro-electricity as providing a power base for industrial development and mechanised agriculture; (2) the produc-

tion of agricultural machinery and tractors and the chemical industry supplying farms with mechanical equipment and fertilisers; (3) the development of such agricultural industries as sugar refining, flour milling, oil manufacture, brewing industry and the industrial treatment of dairy and meat products, fruit, truck gardening, etc., which is of tremendous importance for the development of intensive agriculture and of rational utilisation of agricultural products. The cotton-mill industry has been brought into the cotton-producing belt in Central Asia and Transcaucasia. In the northern part of Ukraine the production of beets and the sugar industry have been concentrated and there are also being developed on a larger scale than before the animal products industry, packing houses, canneries, etc. Cotton mills, silk and woollen factories, cotton-cleaning plants and plants for the production of chemical fertilisers—all seek to extend general economic development and industrialisation in what were in the past exclusively cereal and raw-material regions. The Five-Year Plans were so constructed that there is a shifting of industrial capital in favour of the immature economic regions which are now in the initial stages of industrialisation, their young industries being favoured more so as to show a higher tempo of development than the industries of the older industrial regions of the Soviet Union. In India we have to adopt a similar plan of offering differential advantages in favour of industries in the younger economic regions, losing sight neither of the programme of inter-regional distribution of labour nor of the present economic unbalance and over-crowding in agriculture in the backward regions.

Integration of Large-Scale Organised Industries and Cottage Handicrafts.—Where the highly organised cotton and jute industries cannot be transferred to the sources of their raw materials and the labour market, a constructive scheme will be the introduction of improved cotton and jute carding and cleaning plants, ginning and pressing factories in the countryside. Silk and woollen manufacture, soap and oil, food, leather and tobacco industries may all be developed

in rural areas and the growth of such light industries co-ordinated with the long-established handicraft and cottage industries in the villages. India must plan as in Russia not only the speedy development of the heavy industry but also of the light industries so that these may supply the village and cottage handicrafts with raw materials and half-finished goods for all kinds and stages of cottage production. The revival of handicraft and the advancement of the light industry go together and a better orientation can be achieved through a discriminative protection of light and agricultural industry as well as of handicraft. The development of hydel power is especially to be looked at from the point of view of industrialising the countryside and carrying out an industrial integration between the heavy and light industry, agricultural industry and rural craft, which is now so sadly lacking in the industrial structure in India. Such integration and co-ordination of organised industry and scattered cottage production will effectively contribute towards introducing better mechanical efficiency and marketing methods into many of our moribund cottage industries and bringing about industrialisation at a quicker pace than if handicraft and cottage production be left entirely out of the picture. Planned tariff and excise can eliminate the competition between hand-loom weaving of cotton and silk and the mill industry as these, supported by zoning and other regulations, have limited the scope of small-scale *gur* production and the sugar industry. Tariff against foreign imports may be adjusted on the basis of fair selling-prices of cottage and small producers and a countervailing excise duty imposed on the home manufacture of similar goods by large-scale establishments. The levy of a discriminative excise on khandsari and factory sugar in India represents in fact a principle which is worthy of extension to small, medium-sized and large establishments in several lines of industrial production which are already protected or seek protection in future. The Indian Tariff Board on cotton textile industry has accepted this principle of levying a small cess on power-loom production for creating an All-

India fund in aid of the development of the hand-loom industry. The consumer now pays 50 per cent above the f.o.b. price except in the case of American textile products taxed at the level of 20 to 25 per cent. The Indian cultivator accordingly is forced to pay a price for his cloth much higher than he can afford, especially in the present period of agricultural depression. The Government, it is estimated, now gains only a rupee because of the import duty, while the consumer loses about Rs. 6 for the higher price of cloth goods he buys. Yet the industry has not made adequate efforts towards rationalisation and reduction of the cost of production and towards marketing syndicate and combination which have helped Japan to achieve her mastery in the textile trade in the East. A planned tariff, discriminative excise in favour of certain varieties of textile goods produced by the hand-loom weavers and a quota system designed to secure a judicious balancing of agricultural and industrial interests represent the ideal solution. Hand-loom products now represent about 17 per cent of the total consumption. Besides, the opportunities that hand-loom weaving affords for mitigating rural unemployment have received inadequate recognition in planning the Indian tariff schedule. A variety of cottage industries and workshops, instead of being eliminated can be sustained by both heavy and light organised industries and come to the aid of millions of cultivators-cum-artisans now imprisoned in enforced idleness in under-sized holdings.

The Rôle of Small and Cottage Production in Industrial Development.—Many branches of manufacture are carried on effectively in cottages and workshops in rural areas in Germany, Belgium, Holland and Japan and thus the large-scale industrial enterprise and a widely distributed handicraft and homecraft activity help, instead of ousting, each other. In Germany at least 8 million people, *i.e.*, 12·6 per cent of the total population, derive their living from handicraft work. In Westphalia the development of mining and metallurgy displaced the small-scale extraction and manufacture of raw and semi-processed materials but has now

nurtured the flourishing cottage production of finished cutlery. Similarly the rural cottage industries of watch making in the Black Forest and the production of cheap musical instruments in Saxony and Wurttemberg have been aided by the large industry. In the Black Forest region cottagers, who own small plots of land but cannot subsist only upon farming, produce wooden toys, dolls and bead crocheting, which have wide export markets. In Japan the handicrafts are still more important industrially than the factories and there is a vast number of small workshops which produce some of the highest priced and most distinctive of Japanese goods. The Japanese toy industry is gradually superseding the products of the German small and often rural homework in the foreign markets. Even in the industrial city of Birmingham in Great Britain, at least 50 per cent of the industrial establishments are small-scale establishments which employ less than 50 workers and fabricate semi-processed materials. India is essentially a land of cottage industries and workshops, of craftsmen and hand workers. Only 5 millions represented the figure of labour employed in factories out of a total of 154 million workers and a population of 353 millions in 1931. Small-scale handicraft and cottage production is in India far more important economically than in all European countries and even Japan due to the local demand and taste for special or artistic goods, the hereditary skill and traditions of various groups of rural workers, the isolation of the villages and the seasonal character of agriculture in the country. Hand-loom weavers alone represent 5 million persons, *i.e.*, the total for all kinds of workers employed in the organised industries, and in 1935–36 produced 166 yards of cloth (crores) as compared with the mill production of 350 yards (crores) and 97 yards (crores) of imports. No separate figure for handicraftsman and cottage workers exists in India, but an analysis of the census occupational data yields 10 millions. This excludes those who are carrying on some crafts as an occupation subsidiary to agriculture. A U.P. Census of subsidiary occupations which was undertaken systematically for the

first time in India revealed that out of every 10,000 total population, 104 returned a subsidiary occupation of an industrial character. Accepting this proportion for the whole of India we estimate 4 million persons as engaged in industrial subsidiary occupations. This brings the figure of persons engaged in handicrafts and cottage production to about 14 millions, and is probably an under-estimate. There are quite a large number of cottage industries and handicrafts which produce for an Indian and even overseas market rather than for local consumption. Industrialisation will not mean complete mechanisation in the country. The immense variety and tenacity of cottage arts and handicrafts and a dense handicraft population are themselves brakes on mechanisation. In Soviet Russia, where the combination of the farmer and the craftsman is extremely important as in the national economy of India, the Five-Year Plan has given a great deal of emphasis to the development of handicraft and the promotion of Co-operative Societies and government agencies which supply the artisans with raw materials, semi-manufactured goods, machinery and tools and also take charge of distribution of finished wares. In Japan a new movement has been started to spread mechanical industry throughout the countryside on the basis of two concerted plans, first, to process farm products on the farms, and, secondly, to divert part of the mechanical industries from the urban centres to the villages, and utilise the surplus labour in agriculture. In a country like Japan, where the artisan groups are endowed with a rich dower of manual skill and artistic delicacy, rural labour has been found to attain a high efficiency in quality production by operating machinery. The same will probably hold good in India, provided that complicated mechanical work can be similarly divided into simple and uniform operations for the purpose of the rural workers. As in Japan so in India the high standard of excellence reached by rural handicrafts augurs well for efficiency in certain branches of specialised, mechanical work in the countryside. Industrial planning in India must have as one of its primary objectives the co-ordination of

small and cottage production, workshop or middle-sized industry and the big organised industry. Each has its peculiar scope under the special conditions of Indian social economy and cannot be disorganised or superseded without economic inefficiency, wastage and social unsettlement.

Tariff *versus* Increase of Purchasing Power of Agriculturists as Aid to Industrialisation.—With the increase of population the proportion of the so-called industrial workers to the total population has steadily diminished in India. Even a forward industrial policy backed by protectionism of an extreme kind cannot materially alter the basic trend of India's national economy. For several decades we shall not be able to deflect more than 5 to 7 per cent of the total population to the big organised industries though heavy tariffs may entail for the agricultural community an excessive burden, which of all sections in the country they can least afford to bear, especially in a period of slump of agricultural prices. On the other hand, if we continue to increase this burden by high tariffs for nourishing industrial development, we may be killing the goose that lays the golden eggs. Ireland has not been able to make much headway in the development of new industries in spite of her newly acquired fiscal autonomy. As in the case of India, Eire's industrial advance is limited by the low purchasing power of her agriculturists, representing more than 75 per cent of the population, and her fiscal independence has been unable to diminish much her dependence on foreign imports of manufactures, or overcome the inherent drawbacks of her economic structure acting as a brake on her industrial progress. The income of agriculturists, which constitutes the principal demand for the output of the protected industries, has recently diminished, and is partially dependent even at its reduced level on the continued expenditure of public money on bounties, subsidies, employment and assistance. In many of the protected industries saturation point has been nearly reached as in India, while they can never hope to supply for a foreign market. A Banking Commission which have recently reported have concluded that in the absence of

an increase in the national income even a very pronounced industrial policy will not bear much fruit. This should have a warning lesson for India particularly because the advantage of an extensive internal market for home manufactures is largely offset here by a much lower purchasing power of the masses, largely agricultural. Cultivators working on uneconomical two to three-acre holdings have not only little surplus for spending on manufactured goods but are bringing down their purchasing power by excessive multiplication. It is this low purchasing power which explains largely the fact that three of our major industries, *viz.*, sugar, jute and cement, are now faced with over-production. With the establishment of the new works at Hirapur, the iron and steel industry will also be faced with an inelastic market. To-day the supply of capital in India exceeds the opportunities for conservative investment. And yet instead of attempting industrial enterprises in new fields which may diminish our dependence on a thousand foreign imports and the large export of important agricultural raw materials, we think of industrial progress chiefly in the lines of established industries. Industrial production tends to imitate rather than venture on untrodden lines. Not to speak of the heavy chemical and engineering industries, which alone can initiate an all-round even industrial advance, India has made little headway in the agricultural industries like cotton gins and presses, rice, oil and paper mills, which are too few in number, nor in the preparation of food stuffs, synthetic dyes, toys, shoes, rubber goods, film equipment, and glass manufacture, to mention only a few products for which we are dependent on foreign countries.

Poise Between Agriculture and Industry. — The State policy of industrial development, accordingly, should be directed on a four-point plan: firstly, consolidation and rationalisation of the big organised industries now threatened by over-production and cut-throat competition; secondly, co-ordination of the policy and measures of the different Provincial and State Governments in respect of

particular industries, control of prices of raw materials, wages and conditions of labour, which should be settled on a federal rather than on a provincial basis; thirdly, elimination of competition between the big industry and handicraft and homecraft and integration of cottage, workshop and factory production, representing links, subsidiaries and auxiliaries in the process of manufacture; and, fourthly, selective protection of those large agricultural and light industries which may make small-farming more remunerative and at the same time deflect surplus labour from agriculture and the land or diminish agricultural semi-idleness or unemployment. The remarkable expansion of the sugar industry in India, which reduced the imports of sugar from about a million tons in 1930–31 to only 23,100 tons in 1936–37, gave to the cane-growers of the U.P. about Rs. 6 crores and those in Bihar about Rs. 3½ crores for cane crushed in factories, provided seasonal employment for about 200,000 villagers and benefited all grades of agricultural interests, is a stimulating example of an appropriate agricultural-industrial adjustment and planning. The development of the leather and oil-crushing industries in Madras, the former producing tanned (not dressed) skins and hides for export and the latter manufacturing oil and oil-cake and utilising the latter as valuable manures, formerly lost to agriculture, are other heartening examples, though on a very much smaller scale, of sound planning. For many years over 20 per cent of India's total exports, in weight and in value, consisted of oil-seeds, after all the home demands were met. Due in large measure to the development of the chrome tanning process and the Ottawa pact, the export of chrome leather supplied to Great Britain has increased fifteenfold in the course of the last 5 years; while the manufacture of boots and shoes in the country has also increased resulting in the diminution of imports from 5·2 million to 1·2 million pairs between 1929–30 and 1937–38. The expansion of soap and paint industries is even more remarkable. The present output of soap in the Indian factories, estimated at 70,000 tons, generally using cocoanut oil, represents an increase of about 250 per cent

as compared with pre-war years. Between 1929–30 and 1937–38 the imports of soap declined from 343,460 cwt. to 41,538 cwt. The paint industry, which utilises another valuable secondary crop, *viz.*, linseed, that is not inferior in quality to any produced elsewhere, now produces approximately half a million cwt., representing two-thirds of the Indian consumption. Here again the imports have been reduced from 416,531 cwt. to 278,514 cwt. between 1929 and 1937. It is noteworthy that in these industries the facts contributing to their development are less tariff assistance and more the recognition that the primary raw materials used by them are available from agriculture and can be efficiently utilised through local scientific research and technology, and that the idle labour in the countryside can be easily trained for semi-skilled work in these establishments. Agriculture and the agriculturist have gained considerably from these. With heavier population in India it will be uneconomical to grow more oil-seeds for exporting them either raw or in the form of cakes, as this would mean a serious drain of nitrogen. On the other hand, with formidable rivals like the Argentine in the supply of linseed, China in the production of sesame, and Rumania in the supply of rape-seed, with the difficulty of supplying uniform and reliable products for the European industries and with applied chemistry constantly discovering new substitutes for old products, it would be on the whole advantageous to develop a large indigenous oil-crushing industry in the country. The cake would mostly be used up in the fields and consumed by the cattle, while the vegetable oils and fats would support the growing soap manufacture and such industries as the production of paint, varnish, linoleum, ink, illuminant and lubricant for heavy machinery. Planned industrial development would utilise large quantities of secondary crops and raw materials now being exported and aid towards better and more remunerative agriculture, while the diffusion of science and technical skill and the engendering of new wants and attitudes among the cultivators that rural industrialisation fosters, would be as far-reaching in its social effects as the

balancing of the national economy firmly poised between agriculture and industry. Subsidies, regulation of production and of prices of cane, jute and oil-seeds, for instance, export duties on certain secondary crops, trade agreements and the price-raising quantitative control of home production and exports may each or all be necessary in this connection and thus the Indian farmer, like the Irish or the Japanese farmer, should be in possession of an almost complete battery of economic weapons. India may easily take a leaf from the Irish economic policy in restricting the output of those crops for which foreign markets have shrunk to such an extent as may be necessary to secure remunerative prices for the producers, and at the same time enter into bilateral agreements with such foreign countries which are prepared to take our agricultural products in exchange for their manufactured goods. India's formidable rival in the exploitation and capture of new markets in Africa and South-eastern Asia for her industrial products is Japan, and it is well known how depreciated currency, low wage costs, directly subsidised exports, the link-system and barter arrangements, and the policy of State monopolies and quasi-monopolies have helped Japan's recent trade expansion.

India has to emulate Japan for specially encouraging export industries by rationalisation, commercial agreement and subsidy and adjusting the monetary policy to the needs of such industries with a view to capturing overseas markets, as, for instance, for her cotton piece goods, jute and pig iron, where the Japanese hold has, as the result of the China war, lately weakened. With reference to India's cotton goods it is necessary that in seeking new avenues for exports, the interests of the producers of raw cotton will not be overlooked. The general principle of bilateral textile agreements that the textile trade will be shared by exporting countries in proportion to their imports of raw cotton will have to be modified in the interests of Indian agriculturists on whom the greater portion of the burden of the high tariff falls. It is these latter dominant agricultural interests which preclude an agreement relating to the quota of Lancashire cotton imports on the basis of mere

assurances and goodwill as regards the purchases of Indian raw cotton by Great Britain. With Japan expanding cotton cultivation in Manchukuo and China for her home manufacture, her demand for raw Indian cotton is bound to be reduced. This will hit hard the Indian agriculturists in the absence of either rationalisation of Indian power-loom production or reorganisation of hand-loom weaving. At present cotton mills in India, it is estimated, are producing 60 per cent of their capacity and yet new mills are being established. If the export trade of Indian mill-made goods does not improve, there will be more curtailment of production, more industrial employment and more blocking of capital, which needs to be directed into new industrial enterprises, while the economic position of Indian cultivator who will not find an alternative market will also deteriorate.

Planned Money.—The agricultural countries of the world have attempted to insulate their internal economic structure against the economic depression by planned monetary control. They have aimed at reflationary stabilisation of internal prices in order to maintain costs-prices equilibrium even at the expense of exchange-stability by means of devaluation combined with controlled internal reflation. But in India the fetish of exchange-stability at all costs has been permitted to transmit the devastating deflationary shocks of the world economic depression to our internal economy. The result has been that India has gone through the travail of a grinding price deflation which has brought about a slow paralysis of economic life. This deflationary pressure has exerted itself particularly severely upon the agriculturists owing to the sharp fall in the prices of agricultural products in terms of industrial products, resulting in the virtual insolvency of the masses of the population. The present recession in trade, which started after the collapse of the short-lived boom of 1936, is accordingly bound to shatter the fabric of India's agricultural economy more completely than many people imagine unless bold measures are taken to prevent further deflationary pressure through

the present ratio. It seems, therefore, that in the absence of a rationally planned money all programmes of economic reconstruction and recovery will encounter a stone wall.

With planned money, control and co-ordination of various kinds of credit agencies in the country, not merely will the money rate be freed from the present violent seasonal fluctuations, which hinder the development of trade and industry, but the banks' service to agriculture, now under the crushing burden of debts incurred at usurious rates, will become the touch-stone of their expansion and stability. Rationally planned currency and rural banking, under the control of the Reserve Bank, will facilitate the movement of goods and money from the villages to the cities and *vice versa*, eliminate the present disparity between harvest prices and normal prices, between rural and urban price-structures and money-rates, and also mobilise capital resources, which are lying about in pools scattered all over the country in the form of hoards. These measures which seem so essential for the recovery and stabilisation of prices are being delayed because credit and banking, unlike industry, cannot be created in a day. But no doubt India's handicap that she does not enjoy complete control over her monetary policies prevents in no small measure monetary rationalisation and the establishment of her internal cost-prices equilibrium.

Inter-Dependence of Planning in Different Sectors of Economic Life.—Yet without these, agricultural prices will not recover, nor real wages and standard of living of the great mass of agriculturists rise. The standard of living of the masses can improve only in the following manner: maintenance of cost-prices equilibrium in agriculture and increase of agricultural income; opening out of subsidiary sources of employment in handicrafts and agricultural industries in the countryside; reduction of birth-rate; equitable distribution of national income and revision of the tax system; and improvement of foreign trade by reciprocal agreements, for the special advantage of the agriculturists. In so far as each one or more of these are delayed

industrialisation will be tardy. For it is the peasant's income and effective demand for industrial products which hold the major key to India's industrial advance. On the one hand, an amelioration in the standard of living of the cultivators and general rise of purchasing power alone can effectively speed up industrialisation and at the same time slacken the present rate of multiplication. On the other hand, the development of agricultural industries can enable the agriculturist to obtain remunerative prices for the cultivation of raw materials and industrial crops, release the excessive pressure on the soil, mitigate agricultural unemployment and improve both agricultural efficiency and income, thus laying the foundation for an all-round improvement in the standard of living. In order to counteract the vicious circle of subsistence farming, low standard of living, poor purchasing power, and industrial backwardness, the attack should simultaneously begin from the agricultural front with improvement of farming methods, practices and organisation and from the industrial front with the stress of rural industrialisation. Nor can the social front be neglected. For neither agricultural nor industrial planning nor devising better land and tax systems with a view to diverting a larger share of the national dividend to the poorer strata of the population can succeed with such a storm of breeding as has increased the population from 353 to 380 millions between 1931 and 1938. With a slackening of population growth any economic planning can bear fruit more quickly.

"Balances" and Synthetic Indices for Checking-up Economic Planning.—The chief aims of a Five-year Economic Plan in India should be accordingly: crop and food planning and a coordinated technical reconstruction of agriculture, forestry, soil and river management; the extensive development of key, light and agricultural industries; rationalisation of money and credit and the maintenance of cost-prices equilibrium; and the elevation of the peasants' standard of living and population restriction. It is inevitable that there will be different plans for different regions and

Provinces although there is large scope for co-ordination and integration of the activities of different Provinces. Co-ordination is the key to economic planning: co-ordination between regions, between agriculture and industry and between all the sectors of economic life. Agricultural reorganisation depends on rationalisation of marketing and credit, on industrialisation and on planned money and price level. Industrial advance rests on the increase of purchasing power of the agriculturists, and the technical skill of the workers, on tariffs and commercial agreements, on banking and transportation facilities. The reform of the land system cannot succeed without an increase of agricultural yields and without industrialisation which may draft off the surplus labour from the land; nor can the literacy drive make much headway when population multiplies. And so on for every branch of the national economy. This would demand that the National Planning Commission, which India has constituted, should work on the basis of a system of checks and balances provided by certain measurable and synthetic indices, which establish a specific co-ordination between two moving indices: for instance, the correlation of permanence and heritability of rights of tenants and increase in agricultural yields; the correlation of expansion of cottage and agricultural industries and the decrease of small tenants and the floating landless class; the correlation of increase in agricultural yields and subsidiary employment and in the purchasing power of the masses; the correlation of increase in purchasing power and in wages and standard of living and the decrease in birth-rate; the correlation of increase in wages and the standard of living and in productivity of labour; the correlation of increase in productivity of labour and the decrease in cost of production; and so on. The Gosplan in Russia draws up such general "balances" for shaping and appraising the internal structure of the plans and for apportioning and co-ordinating their component parts. Statistical schedules adapted to planning schedules prepared by each economic unit of the country will represent the exact inductive basis of the accounting, checking up

and control of economic planning. The preparatory materials for planning should be worked out in detail in the Provinces in Conferences consisting of economists, technical experts, representatives of single industries, etc. Among the subjects at such provincial Conferences which should appropriately be taken up at once are: soil and agricultural survey and the demarcation of zones of specialised and commercial cropping; soil conservation and afforestation; flood control, canalisation and river management; water transport; improvement of cattle, dairying and the problem of elimination of uneconomical stock; the rehabilitation of the co-operative movement; debt liquidation and improvement of crop finance and marketing; the problem of revision of land settlement and reform of tenancy; the geographical redistribution of industries; electrification; utilisation of mineral resources; the manufacture of machines, steel rails, locomotives and motor-cars; the chemical industry; the reflationary stabilisation of internal prices; the linking of indigenous credit agencies with the organised banking system; the development of Indian shipping and coastal traffic. It is only after meticulous and prolonged practical discussions by experts that well-balanced plans can be fashioned in the Provinces, and then an all-embracing "pyramid of plans" broad-based on the regional and provincial plans can be built up for India.

Ideology.—Planning need not assume a fundamental reconstruction of the economic system in India; socialism or communism is not the *sine qua non* of planning. Nor does planning demand a dictatorship. Even in Great Britain with freedom of competition and ownership of property much has been achieved through planning subsidy and price insurance methods in the field of agriculture. A determinate and measurable economic goal can be sought more effectively by a greater integration of agricultural, industrial and monetary policies. This is really the crux of modern economic planning. Research, organisation, technology and legislation, all will have to direct constantly the

mechanisms of the general economic advance in full co-ordination. The object of planned economy for India is neither economic autarchy and national aggression as sought in the Fascist countries nor economic imperialism, based on the power and prosperity of a small capitalistic and directive class, as in the democratic countries, nor again, a bare materialistic and regimented culture as in Soviet Russia. The ideology behind economic planning in India is, according to the present writer, the broadening of the economic base of a peaceful agricultural civilisation for the purpose of national self-defence, on the one hand, and the full and free expression of her ancient moral and social virtues in the changed economic world, on the other.

PART IV

INDUSTRY AND LABOUR

CHAPTER XVIII

ORGANISATION OF COTTAGE INDUSTRIES AND HANDICRAFTS

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Classification of Handicrafts.—Cottage industries and handicrafts in India may be broadly divided into four classes:—(A) Peasant arts and crafts carried on in the slack seasons of agriculture and meeting usually household requirements, but occasionally utilising local reed, grass, bamboo, clay, wool, cotton, etc., for an extended market; (B) Village subsistence industries indispensable for the agricultural routine carried on by the village smith, carpenter, potter, etc., in the self-sufficient village communal organisation; (C) Village art industries carried on by handicraftsmen representing a higher standard of local art and creativeness and commanding district and sometimes overseas markets; and (D) Urban arts and handicrafts representing even superior organisation of craftsmanship many of which still persist or thrive in the modern industrial world.

(A) Peasant Arts and Crafts Subsidiary to Agriculture

Where Craftsmen are Cultivators.—There is a large variety of cottage industries in which the agriculturists of India are engaged during their off seasons, which serve, so to speak, as a second string to their bow, supplementing the main occupation when there is no work for them either at home or outside. In the Punjab and United Provinces the peasant is occupied outside the more intensively cultivated areas for not

more than two hundred days. In Madras the peasant on a single-crop land works for about only five months in the year and on the two-crop lands for about eight months in the year. The period of agricultural work in Bengal and North Gujerat, taking a normal day of seven hours, is about the same. On account of the present excessive fractionalisation of holdings and the lack of facilities of irrigation, agricultural employment, even in the busy months of the year, is not continuous. Thus the mass of peasants follow subsidiary occupations whose number and variety are larger than are ordinarily supposed. Among the important cottage industries widely pursued by the Indian peasants are hand spinning and weaving, *gur* making, flour grinding, rice pounding, cotton ginning, rope making, basket making, mat weaving, sericulture and tobacco manufacture. Home consumption, sufficient demand, and inadequate communications have all contributed to maintain such handicrafts in their crudity and simplicity unaffected by modern progress in either industrial art or economic organisation. Yet the crafts show tenacity as well as capacity of availing themselves of raw materials on the spot, while transmitting through the ages a natural dower of manual skill and aptitude.[1]

Specialisation.—Of the types of cottage industries which are associated closely with agriculture, hand spinning is by far the most important. Though reliable figures cannot be obtained, the amount of cotton spun by the Indian agriculturist in his cottage is still considerable, while in the mountain villages the home-spuns have acquired a distinction which often travels beyond the locality. Recently there has been a considerable expansion of hand-spinning due to the activities of the Congress and the *Khadi* Associations. One rural centre in Bihar alone produced in 1938 *khadi* worth more than Rs. 1¼ lakhs, and distributed 1,000 spinning wheels. The majority of spinners come here from the landless classes, who are idle otherwise for more than half the year, and their earnings amount on an average to Rs. 5 per mensem and compare favourably with the local agricultural

[1] *Vide* the present writer's *Foundations of Indian Economics*, Part II.

wages. The activities of the All-India Spinners' Association embraced 13,000 villages in 1938 and the production for the year came to 1 crore 23 lakh yards in 1938. The number of registered spinners and weavers was 286,000 and 18,000 respectively. The earnings of an average spinner varied from 6 as in Maharasthra and Gujerat to 2 to 3 as in the other Provinces for eight hours' work. As a rule, it is the women who spin while their husbands weave, but sometimes custom decrees a contrary division of labour. Thus in the Kumaon hills the men spin almost unceasingly, while it is the women who weave. On the other hand, in a plains district like Etawah in the United Provinces the women are seen to weave cloth and the men to size it. In Assam also practically every peasant woman in the valley plies her loom and it is she who meets the clothing demands of the household. There are as many as 421,367 hand-looms in the province according to the Census Commissioner of 1921, who adds that "there is here an average of nearly one loom to every two occupied houses. Weaving is an established custom of the housewife, and cloth is nearly always made for home use." It is because in many provinces along with the specialised caste of weavers a considerable proportion of the agricultural population is engaged in weaving that about one-third of the cotton cloth consumed in India as a whole is produced by the hand-loom. The proportion is much higher in the agricultural provinces. In Bihar and Orissa, for instance, the hand-looms supply even 40 per cent of the consumption of piecegoods in the province. Hand-loom weaving supports roughly 5 million persons in India and its output is valued at about Rs. 500,000,000[1]. The relative *per capita* consumption (million yards) for 1933–34 was as follows: hand-loom production, 4·00; mill production, 8·03; and imports 2·14. That the hand-loom weaving industry in India is not losing ground is indicated by the fact that the quantity of yarn annually consumed by the hand-loom weavers increased from 255 million pounds during the ten years ending 1924–25 to 344 million pounds during the ten years ending 1934–35, the increase being 35 per cent. In

[1] H. L. Dey, *Indian Tariff Problem*, p. 64.

the Punjab and in Bihar and Orissa, the value of cotton cloth produced annually on hand-looms in cottages is about Rs. 50,000,000. Madras, however, with its 170,000 hand-looms working and employing about a million persons, takes the lead in cottage weaving, producing about one-third of the total hand-loom production in India. The total consumption of cotton yarn by hand-loom weavers in this Province increased from 59 million pounds in the decade ending with 1921 to 73 million pounds in 1933. Even in an industrialised province like Bombay there are as many as 1,000 weaving centres, employing roughly 80,000 hand-looms. 123,893 persons are engaged in spinning, sizing and weaving cotton in the cottage, of whom 52,398 are women, mostly hand spinners. Bombay has a special advantage in hand-loom production. In Northern India the price which the hand-loom weaver has to pay for his yarn is considerably in excess of the price of yarn and the freight from Bombay to the weaving centres. In spite of this disadvantage the largest congregation of hand-loom weavers in one rural centre in India is to be found in Daburhat in the District of Dacca, Bengal, where historic tradition and hereditary skill of weaving castes explain the presence of 60,000 weavers working 20,000 looms in the area. Daburhat may well be described as the Manchester of India. Recently a co-operative industrial society has been established here to supply cheap electricity to the looms and provide facilities for the purchase of yarns and marketing of cloths.

Incidentally it may be mentioned here that in all parts of India among the cottage operatives women dominate in hand spinning, whether it be cotton, wool or silk. When the yarn is bought, women do all the winding and warping and often assist in the sizing of the warps. In cotton ginning, wicker work, basket making, embroidery, needle work, bangle manufacture, seri-culture, coir spinning, rope making and fan making women workers are also more numerous than men. It is only in metal, wood, leather and glass manufactures that the women relegates to the back-ground. A census of the cottage industrialists in Bombay

revealed that the number of women cottage operatives is about half that of men workers.

Leaving aside spinning and weaving and the agricultural industries, such as *gur* making, cotton ginning and tobacco manufacture, or, again, seri-culture, which thrive only in a few favoured localities, the peasants sometimes show a good deal of skill in straw plaiting or basket making, cane work or toy manufacture, rope making or fan making, coarse silk, blanket weaving or making of artificial flowers and thus the fame of a peasant-craft spreads far and wide. Flower gardening and scent manufacture by the Jaunpur peasantry are sometimes carried on in connection with agriculture and have justly obtained a wide celebrity, while the collection and extraction of honey in many hill districts, lac culture and even shellac manufacture in areas adjoining forests are important occupations of agriculturists.

Thus certain trades have specialised in special lines and yet the industrialist here is the peasant. Basket weaving is subsidiary to agriculture in several villages in Jaunpur, Allahabad and Benares districts and basket weaving is by no means a simple craft. The mat industry of Sylhet and Tinnevelly has acquired a reputation which has travelled far beyond the provinces and yet it is an industry which is chiefly in the hands of cultivators. The abundance of palm accounts for the proficiency of peasant coir spinning, wicker work and mat making in Malabar and Southern and Eastern Bengal. Bamboo mats made in Karimganj in Assam are used for lining the holds of ships in the port of Calcutta and for roofing country boats, jute godowns and brick fields throughout Bengal. It may be mentioned that peasant women also play an important part in this industry. It is they who weave the mat while the men prepare the bamboos. In the Assam valley, *muga* and *endi* silk worms are reared on the land, and the housewife often weaves silk cloths, showing great skill in craftsmanship. In many villages of India we find the manufacture of wooden lacquered toys, the preparation of umbrella handles, and the making of baskets, chairs and stools.

An agriculturist who plies a craft during his spare hours

and generally with no help save that of his family is a craftsman, but as a rule his craft is crude and moribund. Still, there are important exceptions to this, as we have just seen, where the craft, though carried on in association with farming, has on account of advantages such as access to suitable raw materials, *e.g.*, special kinds of rush, reed or gras, (*munj* or *khaskhas* in Northern India or *korai* in the Cauvery districts), date palm or bamboo, cotton, silk or wool, clay or pith, or on account of an ancient tradition due to the migration of an artisan stock or the existence of courts, nobles and zamindars in the area, exhibits a standard of excellence worthy of high craftsmanship.

(B) Village Subsistence Industries

Rural Crafts Followed by Artisan Castes.—These are also cottage industries which are, however, in the hands of industrialists proper, having little to do with farming. The village servant class of artisans usually include the blacksmith, carpenter, weaver, oil-presser, tanner and potter who all cater to the simple needs of the villagers and are still often remunerated by shares of grain at each harvest in the village. The village carpenter and blacksmith are more commonly met with than the village potter and leather worker; while the goldsmith is found only in the richer villages. Everywhere the carpenter and the blacksmith's perquisites in grain, which are usually the same, are greater than those of other artisans and menials.[1] The artisans who are not to be found in a particular village or group of villages cater for them by periodic visits and by displaying their wares at the weekly markets and fairs. The weaver is now being squeezed out of his ancestral calling on account of the competition with machine-made cloths; the potter also finds the market for earthenwares shrinking due to the introduction of metal utensils; and the oil-presser is also being ousted from his traditional occupation by the modern product. Everywhere as the traditional

[1] *Principles of Comparative Economies*, Vol. II.

caste occupation of the artisans has become less remunerative, they have turned to agricultural or pastoral employment. The following table gives for the chief artisan classes of the United Provinces the proportion to all workers of earners (principal occupation) plus working dependants, and of earners (subsidiary occupation) who returned their traditional occupation in 1911 and 1931.[1]

Number per mille of workers who returned their traditional caste occupation as:—

	1911			1931		
	Principal Occupation	*Subsidiary Occupation*	*Principal or Subsidiary*	*Principal Occupation*	*Subsidiary Occupation*	*Principal Subsidiary*
Blacksmith .	318	100	418	313	126	439
Carpenter .	415	116	531	403	141	544
Potter . .	432	79	511	365	95	460
Weaver .	505	14	519	428	38	466
Oil-presser .	436	82	518	408	80	488

It will be noticeable that in every case the proportion of workers who have returned their traditional occupation as "principal" has declined, and the decline is striking in the case of the weaver, potter and oil-presser.

The process of de-industrialisation in the village as a result of which artisan classes tend to follow their hereditary occupation as subsidiary is more prominent in some provinces than in others and has to be carefully watched. Yet here and there even a village subsistence industry may show striking skill and efficiency and find a wider market for its products than a village or a group of villages.

The potter from Bengal who brings his earthenware vessels in boats to Assam finds a ready market largely because he is a better craftsman than the Assamese potter.[2] As a rule, however, the village subsistence industries depend for their prosperity or adversity on the fortunes of local agriculture.

[1] *U.P. Census Report*, 1931, p. 409.
[2] *Provincial Banking Inquiry Committee Report*, p. 111.

This holds good also of the village luxury industries. Often do the artisans supply silk cloths, metal utensils, furniture, shoes, and even ornaments to the peasants on credit who begin to pay for the articles purchased after the reaping of the first harvest. Thus village subsistence and luxury industries are both linked up with agriculture. As agriculture improves with introduction of power-driven machinery in the villages as it has done in certain parts of India such improvement can only be stabilised if the village artisans can effect repairs, and stock and fit spare parts. Seldom, however, have the village craftsmen shown a new attitude and acquired a new skill and training in such directions.

(C) Village Art Industries

Specialisation and Distinctiveness of Rural Luxury Crafts.— In many areas in India rural artistic industries have acquired a wide-spread celebrity. Familiar instances are lac and toy manufacture in Budaun, Meerut, Mirzapur, etc. (U.P.), at Bolpur (Bengal), at Chennapatna (Mysore), at Parlakimedi, Kondapalle, etc. (Madras), and in certain villages of Sylhet (Assam); carpet weaving in Mirzapur and Benares; silk weaving in the villages of Murshidabad, Malda, Madura, etc.; metal work in Baidyarajpur (Bihar), Santipur, Bishnupur, Kharar, Khagra, etc. (Bengal), in Karaikudi, Anapurapalayam, Muddanaikenpatti, etc. (Madras); the manufacture of conch-shell bangles and mother-of-pearl buttons in the villages of Dacca (Bengal); artistic clay modelling in Mirzapur (U.P.) and Nadia (Bengal); paper making, manufacture of pith sun hat and helmet, horn, comb, and vegetable dyes in various rural centres.

But it is needless to mention more: this list, which is by no means representative, is intended only to indicate the wide variety of rural luxury industries. Some of these command overseas markets. To give a few instances: *lungis* and *saries* (coloured cloths and scarfs) made at Melapalayam (District Tinnevelly, Madras) are exported to

Malaya and the Dutch East Indies; glass bangles made at Etah, Fatehpur and Firozabad (U.P.) are exported to Persia and Arabia; embroidered cloths woven in the villages of Dacca (Bengal) are exported to Afghanistan, Turkey and Persia for turbans; and silk *Khes* made in the villages of Shahpur (Punjab) are exported to Africa. Chota Nagpur curtains and ladies' dress materials are now finding a European and American market. Every district is found to contain one or more villages where cottage production like cloth and silk weaving, wooden work, gold, silver, brass, copper, bell-metal, lacquer, bamboo, cane, pith, rattan and leather work is carried on to a high standard of artistic excellence and where these articles are sold in the local bazaars or by itinerant dealers who carry these to distant markets.

As the industries develop variety or distinctiveness, the middleman slips in and supplies the artisans with raw materials with the object of obtaining cheaply their manufactured goods. This no doubt ultimately leads to the extension of markets; but isolated and unrelated industries lend themselves easily to exploitation by middlemen. The above tendency is universal. In no village industry can this be better illustrated than in hand-loom weaving which, as we have seen, is the most important of India's rural industries and is at least half as important as the power-loom industry, both in respect of production and value, and many times more important in respect of the employment which it provides. The middleman supplies yarn to village weavers, who are isolated from the larger markets of the Province, and charges rates which often do not bear any proportion to market prices of yarn and his freight charges. Besides, the weaver lacks continuity of employment and has to borrow money both for his household expenses as well as for the purchase of yarn at exorbitant rates of interest. The monsoon season is dull for hand-loom industry, because the rains seriously affect weaving and there is shortage of demand for cloths. A Madras survey has shown that the hand-loom weavers have to manage for four days on the earnings of a single

day. What he lacks, therefore, is a continuity of employment. As he has no marketing organisation he has to sell his goods through middlemen who charge heavy commissions. Finally, his designs are often out of date and he is unable to meet the changing needs and fashions of the consumers and his products.[1] The above picture of the cottage artisan's economic weaknesses is more true of workers other than village weavers, for, while most cottage industries have hardly benefited from the results of technical research and development, some of the appliances which have greatly improved the manipulative processes in textiles, such as the fly shuttle, sley, dobby, draw boy harness, country jackguard and warping mill, have been adopted widely by cottage weavers in various parts of India. Both in Bombay and the Central Provinces the introduction of a large number of fly-shuttle sleys has caused over-production in certain weaving centres and this has affected the weavers adversely. At Chanda in the Central Provinces the weavers attributing all their miseries to the fly-shuttle sleys have in accordance with a caste resolution made a bonfire of them!

(D) Urban Arts and Handicrafts

Development of Urban Handicrafts.—In a town or city there is scope for a wider market and larger variety of production, involving specialisation in industry and trade. The patronage of the nobility, the desire for luxuries among an ease-loving public, the religious obligation to purchase particular varieties of goods, the hereditary skill and dexterity of particular castes or groups of artisans—all these have contributed to the development of handicrafts and industries of luxury. But the economic status of artisans has not improved; indeed, the greater the demand for art wares or the cost of their raw materials, the stronger is the grip of the middleman or capitalist on the artisans and their work. Another reason why the

[1] L. B. Green, Director of Industries, Madras, in a lecture at Madras, August 1935; see also the speech of R. D. Bell, late Director of Industries, Bombay, Assembly debates, March, 1924.

urban artisan is sometimes worse off than the rural worker and tends to fall more and more under the grip of the *mahajan* is that he has no connection with the land on which the latter falls back in difficulty and has to fear the competition of a wider market. If he is manufacturing for export, "he has not the means, the capacity or the organisation to dispense with the middleman."[1]

Types of middlemen in urban handicrafts.—(a) The Itinerent Dealer.—There are thus various types of middlemen. There is, firstly, the itinerant dealer who supplies raw materials to the artisans. The most familiar instance is the trader who supplies yarn to the weaver in his cottage, and gives him piece wages or deducts a commission when he takes over the finished product. In blanket weaving the dealer supplies ready-spun yarn to the weaver and collects from him the finished goods. Even in carpet weaving dealers and firms usually advance cash and sometimes yarn to the weaver, and afterwards take over the finished product. Similarly, the trader in needlework and embroidery goes to the houses of women workers, supplies them with cloth and pays them wages at rates previously arranged. Such dealers either work with their own capital or are agents of larger dealers. Much of the fine embroidery (*chikan*) of Lucknow and some part of its gold and silver thread work (*gota*) is controlled by one or other of these classes of middlemen.

(b) The Karkhanadar as (i) his own financier and (ii) as contractor.—Sometimes, again, the middleman is himself an artisan who has grown rich and employs his fellow artisans either in his own establishment, the *karkhana*, or in their homes. In Benares, for instance, the *karkhanadar* weaver supplies the artisans with the raw materials, gold and silver threads, yarn and dyes, and even with the looms, where they work in the *karkhana*. Some *karkhanadars* are also yarn dealers. Similarly in the metal industry of Moradabad the *karkhanadar* supplies the metal sheets and implements

[1] See *Provincial Banking Inquiry Report, Bihar and Orissa*, p. 92.

to the artisans, whether they work in their own cottages or in his shop, and usually buys these sheets from other middlemen on credit. This also appears to be the system in Benares, where silk weavers are advanced money to the extent of Rs. 40/- and 50/- by the *karkhanadar* who also gives to the former a chit of account. No interest is charged on the amount advanced, but the weaver has to work under the *karkhanadar* until the whole amount has been repaid. The *karkhanadar* so arranges his advances, taking advantage of the weaver's economic helplessness, that the latter cannot easily leave him whenever he chooses. The system works out in the following manner. A weaver usually weaves a *sari* of five yards in five days with the help of his wife and children. He earns Rs. 5/- for a *sari* at the rate of Rs. 1/- per yard. Thus his earning is only Rs. 1/- per diem. But the real drawback of the system is that the weaver who had been paid a lump sum in advance has squandered it and has to live from hand to mouth. The total capital invested by the middlemen in silk weaving in Benares was estimated at Rs. 30 lakhs in 1891, but at present the capital is estimated at Rs. 2 crores and the annual output at not less than 2 crores. Many Punjabi *kshatris* are now taking part in the silk trade of this city. Nearly 50 per cent of the middlemen are working with borrowed capital on which they pay an interest of 9 to 12 per cent and the total borrowed capital may be estimated at 5 lakhs. The capital is borrowed generally from other big middlemen dealers, who also receive deposits in private because of the prestige occurring from an established position in the market.

The position, briefly, is that the *karkhanadar* in some crafts combines the *rôles* of master artisan and financier, and in others is a mere contractor. Indeed, in no handicraft or industry where the cost of materials is high can the artisan or the *karkhanadar* do without the financial assistance of the large dealer or the *mahajan*. Artisans who are habitual defaulters contract debts from two or more middlemen at a time. In some industries, *karkhanadars* take bonds of large sums from workers stipulating the payment of a heavy rate

of interest. In the Moradabad brass-ware industry written bonds are usual and the stipulated rate of interest, which is 3/2/– per cent per mensem, is hardly paid in practice unless the artisan leaves the *karkhanadar* or dealer. In Lucknow, though heavy sums are advanced to the artisans by *karkhanadars*, no interest is demanded. If an artisan leaves one *karkhanadar* for another, the latter returns the sum advanced. In isolated industries in which the artisans are provided materials by the middlemen who purchase their finished products, piece wages, which work out in many cases to inadequate wages for living, are paid. On account of depression in trade, change of taste or competition with foreign products such wages are still further reduced, leading sometimes to the abandonment of crafts for agriculture. In the case of a village luxury industry, however, the artisans whose products have a good sale can command better terms of credit. Thus in the case of the Mirzapur carpet-weaving industry the artisan usually pays interest at the rate of 12½ per cent per annum and his credit varies from three days to one month and occasionally to three months.

(c) **The large dealer as (i) financier.**—The large dealer or *mahajan* is often indispensable in the financing of such industries, such as silk weaving, carpet weaving, gold and silver embroidery, brass, copper and bell-metal industries, manufacture of expensive cotton fabrics, and conch shell, pearl button or horn industries. In certain centres middlemen of this class usually supply raw materials to the *karkhanadars* or individual artisans, but the artisan who works at home is becoming rare in such trades. There is a tendency for the industries to drift from the home to the small workshop as the artisan finds the materials too costly for his pocket or is unable to take risks himself on account of the severe competition with cheap artificial silks and embroidery, machine-made cloths and carpets, enamel, aluminium and porcelain vessels and other wares imported from Europe and Japan. Elsewhere the individual artisan, working on his own account, and the *karkhanadar*, who is

his own financier and undertakes all the risks of the industry, persist. The organisation varies in different industrial centres according to the competition with foreign products or the facilities of credit and local marketing. As public taste is vitiated and the traditional requirements with regard to raw materials, finish of the work and artistic standard fall into disuse on account of the serious competition, especially with the cheap German and Japanese goods, the tendency of the artisans to shift from the home to the workshop, whether of the master artisan or under the thumb of the big dealer and capitalist, is enhanced. In the gold and silver thread manufacture industry in Surat employing about 13,000 workers, 2,000 are independent artisans working on their own account, 6,000 workers work on wages in the *karkhanas* and 5,000 more are dependent, working to order at their own residence.[1] The total value of the gold and silver thread used in this industry is estimated at Rs. 10 million the daily consumption being estimated at 336,000 tolas of silver, and 672 tolas of gold for 300 working days in the year. If we add to this figure the value of silk used, labour charges, etc., the total value of the production in Surat would be nearly Rs. 40,000,000.

The large dealer as (ii) a co-ordinating agent.—In some branches of metal work where the processes of manufacture are so specialised that they cannot be undertaken by the same set of artisans either in their homes or in any *karkhana*, the large dealer who supplies the artisans with the raw materials co-ordinates the different branches of production. His functions, in short, here combine those of the financier and the *karkhanadar*. The brass and copper industry, for instance, is organised in various ways in different industrial centres, such as Benares, Moradabad, Calcutta and Conjeeveram. In such widely different centres as Moradabad (U.P.), Kumbakonam (Madras) and Dharwar (Bombay) wealthy merchants run the workshops, in which as many as a hundred artisans may be employed, usually at piece rates. In most centres the *karkhanadar* works with materials

[1] *Report of the Bombay Provincial Banking Enquiry Committee*, p. 132.

supplied by the middlemen, who are dealers in these wares, employing a few artisans and labourers under him. Sometimes, again, the artisans work at home, obtaining the raw materials either from the *karkhanadar* or the large dealer. But this is becoming rare except in the outlying areas or where the products have not improved beyond a certain standard. Whether the artisan, workshop owner or *mahajan* gains ascendancy or not depends upon various factors such as the supply of skilled labour, the facilities of credit, cost of raw materials and the risk of the business. It should be mentioned that some merchants and most workshop owners belong to the same caste or guild and they do not drive as hard bargains with the artisans as the outside *karkhanadars* or *mahajans* do. In any case it seems possible in any such industrial organisation to get the *karkhanadars* on the side of any scheme of reform, such as introduction of new tools, appliances and designs. Often the *karkhanadars* recruited from the same caste exercise a sort of supervision over families of poorer artisans, whom they may employ with the object of keeping up the reputation for the quality of their goods.[1]

Middleman's Grip due to Irregular Employment and Cost of Materials.—Yet another cause of the prevalence of the middlemen system is the seasonal nature of industry. All crafts such as tailoring, lace, needle work and embroidery work labour under the special disadvantage that they show an exaggerated alternation of overwork and unemployment due to the fact that they satisfy occasional or seasonal needs in India. The lace and needle workers, many of whom are women under *purdah* (seclusion) have no staying power and are completely under the thumb of the *karkhanadar*, who keeps them alive by advances during "the dead season" when the *karkhanas* are not working. It is this which is the principal cause of the prevalence of *bagidary* (arrears)

[1] For the relations between artisans and middlemen the writer has freely availed himself of the materials submitted by him as a member of the Provincial Banking Enquiry Committee. *Vide* his memorandum on the small industries of Lucknow, Report of the Committee, Vol. II, and also Chapter X, Vol. I.

in these seasonal trades. Irregularity of employment, again, weakens the habit of saving amongst artisans who are mostly illiterate; whilst the *karkhanadar*, whose financial position is rarely such that he can afford to lock up his capital during the slack season, is in his turn entirely dependent upon his *mahajan*.

Even where the industry is not seasonal, and the products are in demand throughout the year as in the case of brass or copper wares, the cost of the chief raw materials favours the dealers who even by withholding orders try to sweat the workers in spite of some solidarity on their part hardly to be met among other handicraftsmen. There is a ceaseless attempt on the part of both workers and dealers in this instance to obtain advantage over one another. This is clearly apparent in the seasonal or local fluctuations of wages and prices in an industry which normally ought to be free from these in view of the steady and long period demand of its products. On the whole, the *kothis* get the better of the artisans, especially where they do not confine themselves to dealing in local products but import wares from other centres of metal work, an advantage which helps them to tighten their grip on the local artisans still further.

The Chain of Economic Categories.—We may now classify the cottage industries and handicrafts of India according to their structure and organisation. Speaking of the handicraftsmen in France, Arthur Fontaine, the well-known authority on the small industries of that country, wrote: "Like vegetable and animal species the various economic categories are connected with each other by intermediate links which cannot be classified with any certitude and which help to make of the series of types what is practically a continuous chain." The same chain can be observed in India.

(1) There is the artisan who deals directly with the consumer and works with his own materials. This is generally true of all cottage arts and crafts carried on as subsidiary to agriculture and of village subsistence industries in the hands of artisans who are a part and parcel of the rural community and are paid in shares of grain.

(2) Other artisans though dealing directly with the consumer are provided with material by the latter on a piece-wage system. Familiar instances are village handicrafts in which the materials are more costly or distinctive than usual, wood work and furniture in peasants' cottages, gold and silver work and dress making.

(3) Other artisans receive advances of cash or raw materials from itinerant middlemen who purchase their finished products. This is the most familiar type. Among industries conducted on this system may be mentioned weaving of all kinds, including silk weaving, carpet weaving, and blanket weaving and most village luxury industries where the wares command outside markets.

(4) Some operatives work at home but obtain raw materials from a *karkhana*, which takes over the finished products. Various groups of artisans, such as carpenters, metal and leather workers in all large towns in India obtain their raw materials from shops and *karkhanas* to which they bring their finished wares. Tailoring, lace and embroidery work are often undertaken by artisans and *purdah* women in towns who obtain raw materials from the shops. Village women obtain leaves and tobacco from the *karkhana* in the town and fill in tobacco and pack *biris* (crude cigarettes) at home, which they bring to the *karkhana* every alternate day. Another typical instance is the cottage splitting of mica by thousands of village women in Chota Nagpur. They regularly obtain the mica from the factories which employ them on piece-rates. Various groups of artisans, such as carpenters, metal and leather workers in all large towns in India obtain their raw materials from shops and *karkhanas* to which they bring their finished wares.

(5) Another type is the artisan who works in a *karkhana* under a master artisan (ustad), being supplied with raw materials and often with tools. The *karkhanadar* may himself be dependent on the middle man or large dealer, or he may be his own financier and deal directly with the general public. This organisation is commonly found in shoe making, artistic pottery, wood carving and silk carpet, or blanket weaving. Whenever a cottage industry is in

the hands of a particular caste, it easily assimilates itself to the workshop system; the *karkhanadar*, an artisan himself, provides the necessary tools, employs his caste-fellows on piece wages, and himself arranges the sale of the finished products. It is a survival of the medieval guild.

(6) In some crafts the *karkhanadar* has not risen from the artisan class, but is mere capitalist who has invested his savings in the business. In silk-weaving, in the metal trades and in furniture-making, we often have *karkhanas* run by small capitalists employing hundreds of artisans on piece or daily wages.

(7) Again, the *karkhanadar* may become the contractor or sub-employer working under the large dealers, who advance him raw materials and collect the finished goods manufactured by the artisans employed by the former. This system is found in the lace, the gota, the gold and silver wire and allied industries, to some extent in the silk-weaving industry, in the brass, iron, copper and bell-metal industries in most centres, in durrie weaving, calico printing and in shell, horn and button manufacture.

(8) Lastly, there are industries in which there is no *karkhanadar*, but the dealer or middleman supplies raw materials to the various branches of the industry, finances and co-ordinates the manufacturing processes from stage to stage, and finally disposes of the wares. This kind of organisation is found in certain metal industries.

The Economic Bondage of Handicraftsmen.—Thus a craftsman, whether at his cottage or the *karkhana*, works for the account either of the wholesale dealer or the master workman, and it is this which largely explains his unhappy lot. In most of our small and cottage industries representing one or other of the types of organisation we have noted, the dependence of the workers both for the supply of raw materials and for the marketing of their products is clearly evident, and this dependence usually involves the economic prosperity of the dealer and entrepreneur and sweating of the producers who work for them. Even in non-seasonal occupations like brass or copper work

where there is no alteration between "the dead seasons" (the seasons when the workers die) and the rush season the home workers' position remains as unfortunate as in the case of seasonal trades simply because it is other hands that control the beginning and the end of production. Both for supply of raw materials and the sale of finished products he depends upon others. He may be the master of his own time, but his labour is at the behest of either the entrepreneur or wholesale dealer. His economic position is further weakened by the fact that the metal wares before they are finished have to pass through several batches of specialised and isolated workers, who depend for employment upon the dealer who finances and co-ordinates production.

The same is true of the metal industries in Moradabad, Benares, Burdwan and Kumbokonam. We have already seen that scattered, unorganised production is best represented by lace and needle work. The manufacture of gold and silver threads both in Lucknow and Benares shows a similar separation of its branches, with the works in each isolated from those in others and easily exploited by the capitalists and middlemen. On the other hand, in spite of the special disadvantages, which inhere in intermediate production, brass workers in some branches have now transferred themselves from wage-earners into more or less independent artisans, though it is doubtful whether they can long escape from the widespread net of dealers and middlemen.

In the majority of our small arts and handicrafts the control of the middlemen and wholesale dealers is too evident. From the technical point of view the handicraftsman remains a handicraftsman. He works in his cottage alone or with his family or with a few assistants and apprentices. But from the economic and social point of view the handicraftsman's status undergoes complete transformation. The extension of the market introduces the wholesale dealer, who slips in between the producer and the consumer or the master artisan or the entrepreneur on whose account the handicraftsmen work in the *karkhana*

or in their own home. Thus is seen a widespread process in which the handicraftsman is fast becoming a mere unit of labour, a "factory hand" working for the account of a wholesale dealer or entrepreneur who centralises the trade in their products, and furnishes them, oftener than not, with designs and materials, sometimes even with the tools or implements which they use. In the big cities such degradation of independent home-workers into the proletariat has been facilitated by the opening out of national and even overseas markets for some of their products, by the high cost of materials, by seasonal fluctuations in demand and in the case of clothing industries by the helplessness of scattered and *purdahnashin* women workers, who cannot step out of doors either to seek work or to sell goods.

Co-operative Credit and Supply of Raw Materials.—The want of a central buying and trading organisation has been also the chief defect of home production everywhere. Isolated and unrelated cottage industries lend themselves easily to exploitation by middlemen. Throughout Europe the co-operative system as well as central trading organisations are now playing the most important part in the revival and prosperity of small arts and crafts. In Germany the association of small producers buy raw materials in common and sell their products in common. The commodities produced belong to the individual artisans. As long as we do not expect the requisite capital and trading capacity from the co-operative societies themselves the necessity of setting up a special machinery, like the Financing and Marketing Company, Ltd., proposed by the Industrial Finance Committee in the U.P., for the sale of products of the cottage industries is obvious. A noteworthy feature of rural industries in Switzerland, for instance, is that they have organised themselves on the commercial side into a trading corporation known as Kaufarbunda, with branches at Berne, Fribourg, Lausanne, etc. Nor are the banks inattentive to the special needs and conditions of the home workers. The banks lend money to

the artisans on invoices, labour bills or any prospective claim sufficiently recognised. Swiss banks advance money on cocoons, secured by the undertaking that the spun silk shall not leave the spinner's home till the debt has been repaid. The numerous small co-operative banks in Germany generally assist the small artisans, taking careful account of all their circumstances. The establishment of a large number of small industrial banks, as well as co-operative societies, can alone check the exploitation of small artisans by middlemen and large dealers. Weavers and metal workers, cabinet makers and stone carvers, lacquer workers and artistic potters should be encouraged to buy silk, gold and silver thread, brass or copper sheet, wood, stone, slag and cotton through the co-operative societies or through a secondary body to which the society may be affiliated. Advance in cash and capital for sustenance during the slack seasons and for the purchase of necessary materials for their trade may be freely given, and the artisans should be discouraged from selling goods independently and encouraged to sell them to the societies which are offering them the valuable material service. Similar societies of weavers, metal workers, leather workers, wood workers, potters, lacquer and cane workers, etc., have been organised and are co-operating with good or ill-fortune in the various Provinces of India, success or failure depending entirely upon the elasticity of such societies and convenience they afford to the members. For the chikan workers a co-operative society, after the model of that in Brussels or Palermo, will be a godsend. The Co-operative Society of Women's Work (Le Labour Feminin) in Brussels consists of poor middle-class women, producing objects of art and fancy by home work and selling through a shop which is financed by philanthropists. The capital is 5,000,000 francs. A dividend is paid on share of workers. The Women's Co-operative Society (Co-operative Industries Femininli) of Palermo consists of nearly 300 War widows who make lace, linen-clothing and ornamental chairs. Along with a dividend paid on share, a bonus on goods supplied and sold may be given.

In those industries where the *karkhana* system has come into greater vogue and we have the master craftsman securing work and employing a large number of artisans in his shop the Co-operative Production Society, as in Germany or Italy, will represent a higher level of organisation and industrial development. Thus co-operative societies among silk weavers, cabinet makers, carpet weavers, gold and silver thread operatives, calico workers, copper and brass workers, clay modellers, mat weavers, etc., with a common workshop, and undertaking contracts and distributing the work amongst their members will represent a more effective integration. As we have quite a variety of types of economic relationships in small arts and crafts which show a more or less continuous chain, the co-operative advance will have to exhibit a similar adaptation to the various economic categories and relationships, rescuing everywhere the small artisan from the intermediary or large dealer and gradually leading industry to a greater mechanical and business efficiency and yet on a more equitable basis of distribution of wealth and opportunities than what large scale capitalistic production may permit. Popular banking is the chief method by which the world process of the degradation of workers into automatons in great or small products alike may be effectively combated. A financing and marketing corporation like that working in Switzerland and what is proposed recently for the United Provinces and the co-operative artisans' societies could work side by side with the industrial banks, and thus facilities of long and short-term credit, proper control of credit and supply of raw materials and appliances and expert advice in and effective organisation of marketing would establish the handicrafts on sound business footing.

State Aid for Handicrafts.—Apart from the facilities of credit and marketing which industrial banks and co-operative artisans' and sale societies and a marketing company or emporium can afford, State aid may be a great lever of uplift of the handicrafts in the following manner:—

(1) Municipal legislation prescribing certain minimum

sanitary cottages, conditions and standards in small workshops and industrial establishments where more than five workers are assembled for industrial labour.

(2) Imposition of protective duties in favour of certain long-established arts and handicrafts which employ a considerable proportion of industrial labour. Silk weaving, toy manufacture, artistic clay modelling and metal handicrafts, for instance, need protection by means of tariffs. On the other hand, the increased import duty on cotton yarn falls as a burden on hand-loom weavers. This is only one indication of the necessity of co-ordinating a policy of discriminative protection as between the diverse requirements of cottage industries and large-scale factory establishments. Bengal, Bihar, Orissa, Assam and Madras are the provinces where hand-loom weaving plays a more important part in the economic life of the people than in other parts of India. It is these provinces which have been especially affected by the enhancement of the duty on yarn, which favours the Indian cotton-mill industry.

The Madras Government recently suggested that a cess should be levied on every pound of yarn manufactured by the Indian cotton mills, the proceeds to be utilised for the development of the hand-loom weaving industry. The proposal received the commendation of the Tariff Board. The Government of India for some years gave grants-in-aid to local governments for assistance to hand-loom weaving industry to the extent of a sum of about Rs. 5 lakhs annually.

(3) Concession in railway or steamer freight for certain hand-made products.

(4) Reduction of seigniorage fees on such forest products as special kinds of wood, cane, grass, reed, rattan, etc., as well as horns used in some handicrafts.

(5) Cheap supply of electricity in connection with hydro-electric schemes for rural industries, which at present are being worked by man-power or with costly engines.

(6) State guidance to handicrafts in the selection of designs and processes, assistance in obtaining suitable tools, in marketing, in the diffusion of market intelligence and in

the advertising of their wares. Sleys, tape-weaving looms and calendering plants for the weaving industry and polishing and nickel plating outfits for the cutlery industry have been supplied among other industrial appliances in some Provinces on a hire-purchase system to artisans.

The Home Industries Institute at Mysore, the Bengal Home Industries Association, the Gulzarbag Institute at Patna, the Victoria Memorial Industrial Institute at Madras, and the Arts and Crafts Emporium at Lucknow have recently done a great deal to establish contact between the products of cottage industries and handicrafts with their markets not only in India but abroad.

Need of Co-ordination and Planning.—There is no doubt that the Industries Department in each Province could expand its activities in various directions. Firstly, it should be used as a bureau for imparting commercial and technical information both to the handicrafts themselves and to the trade. Secondly, it should assist in the introduction of approved designs prepared by the technical or art schools. Thirdly, it should be responsible for the adequate advertisement of all artistic products. Lastly, a Provincial Arts and Crafts Emporium under the Industries Department should be established and should act as the headquarters of a system of sale depots, of which there should be one in all important industrial centres and towns, and even abroad such depots may be branches of the Emporium. They may be shops managed by the State or they may be entrusted to the care of existing firms on a commission agency basis.

Each Province has its Co-operative and Industries Departments, but everywhere there is lack of co-ordination in their activities which touch the crafts and lives of the artisans. Through more systematic and co-ordinated efforts they can render valuable service to the handicrafts in each Province.

The Development Commissioners in England recently reported that the magnitude of the results achieved in Germany in the development of rural industries was due not so much to coercive action on the part of the State

in shepherding these industries, or to any direct or indirect assistance from tariffs as to the steady and strenuous diffusion through specially created services of advice, information and education. Many industries, however, were created by State-aided action; for example, watch-making in Saxony and the making of pencils in Bavaria. These new industries have been introduced on a large scale in those districts where such introduction was most advantageous. A system of farming combined with industry, which gives regular employment throughout the year, enables the agricultural countries of Europe to maintain a density of 200 to 300 persons to the square mile. In considerable parts of India, where the density is twice or thrice higher, and where agriculture cannot normally employ the population for more than seven months in the year, the need of rural industries as a subsidiary occupation to agriculture is far greater. For a stay-at-home population like ours enforced idleness during a year of scarcity is a paradox, indicating the lack of balance of occupations in the Indian village which it is one of the major aims of industrial planning to remedy.

The finance of cottage production is in many respects as exploitative as agricultural finance. Local capitalists and itinerant dealers supply credit on hard terms in both cases. To both the artisans hypothecate their wares as cultivators hypothecate the produce of the fields. Methods of finance and marketing are inter-linked and can be supplanted only gradually. The co-operative movement, whether its energies are directed to supplying credit or for providing facilities of supply of materials or sale, must include within its scope the subsidiary as well as the main rural industry, for the two are inseparable.

CHAPTER XIX

INDUSTRIAL DEVELOPMENT

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I. A General Survey

The Antiquity and Excellence of Indian Industrial Arts—Even before the dawn of civilisation in Western Europe, the birthplace of modern industrialism, the manufactures of India were in a flourishing condition. The skill of her craftsmen in the production of highly artistic and delicate cotton and silk fabrics, the working of metals and precious stones, and in all kinds of technical arts, has from ancient times evoked the admiration of the world. The Chinese travellers who visited India in the fourth and the sixth centuries, Bernier who visited India in the reign of Shahjahan, and Tavernier have left glowing descriptions of the marvellous products of Indian arts and industries.

Although insignificant in volume in comparison with modern figures, foreign trade in these manufactured goods played a not inconsiderable *rôle* in the economic life of India. To the dismay of foreign countries, the most significant feature of this trade was the one-sided importation of precious metals into India. Western Europe was brought into touch with Indian goods principally through the Crusades, and from that time onward a considerable traffic, sometimes wholly by land and sometimes by both land and water, developed to the eastern end of the Mediterranean. In the fifteenth century the Mediterranean contact was cut off by the Turks, and the European powers began a frantic competition to discover another route. This led, at the end of the century, to the discovery of the sea route to India by way of the Cape. For about a century

after the arrival of the Europeans, trade was generally in the hands of the Portuguese and the Spanish. The merchants of England viewed their trade with envious eyes, and formed the East India Company; by the opening of the seventeenth century the Portuguese, the Dutch and the English were participating in the Indian trade. At first the enterprises of the British East India Company were merely voyages in which several merchants were associated. About 1657 the Company became a permanent corporation when "factories" were established and regular trading and warehousing begun.

The decay of Indian arts and crafts.—The subsequent fate of the Indian handicraftsmen is too well-known: the political power won at Plassey was now deliberately employed to discourage the manufactures of India by the imposition of prohibitive import duties and other means; and this continued to be the settled policy of England towards India for fifty years and more. Meanwhile the industrial revolution had worked itself out in England, and the destruction of the Indian industries was complete. The inevitable happened, one industry after another succumbed, bringing destitution and desolation in its train. Throughout the nineteenth century the indigenous industries tended to decline, forcing more and more of the population into entire dependence on land.

After the assumption of direct rule by the Crown in 1858, the doctrine of *laissez-faire* was extended to India. The belief gained ground that India with her fertile soil and trying climate was more suited to the production of raw materials to be exchanged for the manufactured goods of English factories. As early as 1788 the East India Company began to take an interest in the expansion and improvement of cotton cultivation in India. Towards the beginning of the nineteenth century the Company resolved to revive the indigo industry and expert planters were brought out from the West Indies for the purpose, and the next fifty years saw its rapid expansion. The tea industry—the premier plantation industry of India—was likewise introduced and

pioneered by the Government. The experimental tea garden started in 1835 was sold in 1839 to the Assam Tea Co., Ltd. Systematic cultivation of coffee was begun in India in 1830.

The rise of modern industries.—By the end of the eighteenth century modern factory industry had been well established in England and during the next quarter of a century was being further developed. By the middle of the nineteenth century England had become the workshop of the world. In India the outstanding industrial events of the nineteenth century were the decay and extinction of indigenous industries, and the rise of one or two modern industries. The earliest form of Indian enterprise was the application of steam to shipping. Gradually steam engines were also being employed in docks, in paper mills, in coining money, grinding flour and in the spinning and weaving of cotton, all in the neighbourhood of Calcutta and by Europeans. The early ventures did not flourish, and for good reasons. Machinery, spare parts and stores had to come by way of the Cape in sailing ships. The engineers, foremen and sometimes even the labourers had to be brought out from England. The regular mining of Indian coal did not commence until 1814: in 1854 there were 3 and in 1880 56 coal mines with a production of 1 million tons. The railway had not come into existence till 1853 when a short line was extended from Bombay; next year a line was opened from Howrah to the Raniganj coal-fields. The construction of this and other railways led to a rapid expansion of the coal industry and the two-million line of production was passed in 1890. By 1900 a yearly output of over 6 million tons was reached; imports had fallen to about 200,000 tons from 800,000 tons in 1880 and exports increased to nearly half a million tons.

With the development of collieries and expansion of railways some initial obstacles to the establishment of modern industries in India had been removed. Barring the ill-started Bowreah mills near Calcutta about the 1820's, the earliest cotton mills appear to have been built in 1854 in the Bombay Presidency by a Parsi gentleman. By the end of 1861, there were 9 cotton mills, and in 1880 there

were 58. The first jute mill was started in Calcutta in 1855, and in 1868 there were 5 of them.

The extent of industrial development.—From these small beginnings India has now become an important industrial country. It is a truism that India is and must remain an agricultural country, but very few realise what great progress India has made in the industrial sphere. Within about 80 years over 2½ millions of persons have come to be employed in modern factories, mines and railways: India to-day ranks as one amongst the 8 leading industrial countries of the world and has a seat on the International Labour office.

In 1935 India had 9,261 large industrial establishments of all kinds employing 1,840,792 persons. The relative importance of the principal industries in India is indicated by the table of employment reproduced below:—[1]

Industry		*Persons employed*
Cotton (spinning, weaving and other)	1935	516,000
Jute mills	,,	281,000
Cotton spinning and baling	,,	180,000
Railway and tramway works	,,	116,000
Rice mills	,,	79,000
Sugar factories	,,	73,000
Tea factories	,,	66,000
Printing and book-binding, etc.	,,	40,000
Jute presses	,,	32,000
Matches	,,	21,000
Dockyards, shipbuilding and engineering	,,	21,000
Ordnance factories	,,	19,000
Bricks and tiles	,,	15,000
Oil mills	,,	15,000
Saw mills	,,	14,000
Rope works	,,	14,000
Cement, lime and potteries	,,	13,000
Tobacco	,,	12,000
Petroleum refineries	,,	11,000
Leather and shoe and tanneries	,,	8,000
Woollen mills	,,	8,000
Dyeing and bleaching and indigo	,,	8,000
Silk mills (including filatures)	,,	7,000
Glass works	,,	7,000
Paper mills	,,	7,000
Coach building and motor-car repairing	,,	7,000
Stone dressing	,,	6,000
Hosiery	,,	6,000
Flour mills	,,	6,000
Kerosin tinning and packing	,,	6,000
Rubber	,,	6,000

[1] Frontispiece to *Large Industrial Establishments in India*, 1935.

Some idea about our industrial development will also be conveyed by an enumeration of joint-stock companies.[1] In 1933–34 the number of joint-stock companies at work of all classes incorporated in India was 9,434 with an aggregate paid-up capital of Rs. 300 crores, of which mills and presses accounted for Rs. 70 crores, plantations Rs. 16 crores, mines and quarrying Rs. 40 crores. The total number of companies incorporated outside India, but which carry on work in India, was 916 with an aggregate paid-up capital of £818 million and debentures of £151 million. Of the paid-up capital and debentures £191 million and £23 million, respectively, were invested in petroleum mining companies, £89 million and £46 million in engineering, £69 million and £5 million in insurance and £57 million in iron, steel and shipbuilding.

The *Capital* index of business activity in India furnishes a very satisfactory standard for measuring industrial activity in this country. The pity is that it does not begin earlier than 1932–33. The recent progress of our industrial production will be best indicated by the table below calculated from the *Capital* index figures.[2]

Industrial Production (*Monthly average* 1935—100)

	Cotton manufactures	*Jute manufactures*	*Steel ingots*	*Pig iron*	*Cement*	*Paper*	*Coal*
Weights	9	6	5	8	5	3	7
1932–33	91·7	90·3	68·2	60·3	67·4	85·0	86·6
1933–34	85·2	90·6	83·4	76·2	73·1	92·4	87·2
1934–35	97·2	95·0	96·7	92·5	88·9	94·3	99·9
1935–36	104·6	101·1	101·9	106·2	101·4	101·7	100·8
1936–37	103·2	124·8	99·7	107·0	113·6	102·4	96·1
1937–38	112·8	129·0	106·8	112·6	130·3[3]	107·5	111·9

In the five years from 1932–33 to 1937–38, the production of cotton piece-goods has advanced by 23 per cent, coal by 30 per cent, steel ingots by 56 per cent, pig iron by 86 per cent, paper by 25 per cent, cement by 94 per cent,

[1] *Joint-Stock Companies in British India*, etc., 1933–34, pp. iv and v.
[2] *Capital*, March 17, 1938, p. 393, and May 26, 1938, p. 777.
[3] Average for 8 months.

and jute manufactures by 43 per cent. And these results were obtained notwithstanding the world's greatest economic depression.

We shall now attempt a brief description of some of the principal organised industries in India.

THE COTTON MILL INDUSTRY

Its growth.—The cotton mill industry is by far the most important industry of India. The rise and growth of this industry will be indicated by the table below:—

Year (ending June 30)	*No. of mills*	*Spindles (1,000)*	*Looms (1,000)*
1851	1	29	
1876	47	1,100	9
1886	95	2,261	17
1896	155	3,932	37
1906 (*ending Aug. 31*)	217	5,279	52
1916	266	6,839	110
1926	334	8,714	159
1935–36	379	9,857	200

The progress and relative stage of development of the industry will be still more explicit from the figures of consumption of piece-goods in India given below:—[1]

Year	*Net imports—yards (crores)*	*Net available mill production—yards (crores)*	*Estimated hand-loom production—yards (crores)*	*Net total available for consumption—yards (crores)*
1905–6	239	61	108	408
1912–17	295	113	104	512
1919–20	99	144	56	299
1929–30	190	229	140	559
1935–36	97	350	166	613

Roughly speaking, the relative position of the hand-loom is almost the same, but the comparative position of foreign imports and Indian mill production has been completely

[1] *Review of the Trade of India* (1935–36), p. 28.

reversed. In 1905–6, imports constituted 59 per cent and mill production 15 per cent of consumption; to-day imports form only about 16 per cent and mill production 57 per cent.

During the earlier period of its history, the spinning section of the industry was more important than the weaving, and more than half of the yarns produced used to be exported. In the present century, however, the forces have been reversed; the export trade in yarns has been practically lost, due mainly to Japanese competition in the East, the expansion of the Chinese industry, and also partly due to increased domestic demand. In 1896 the number of spindles per loom was 106, in 1936 it was only 49. Another recent tendency has been the increasing spinning of yarns of finer counts, and growing importation of foreign cotton for the purpose. Our mills have widened the range of their products, and the improved designs and styles which they have introduced are selling at competitive rates. Dyed and printed voiles, poplins, white mulls, tussores, coloured Italian cloths and poonjees, formerly mainly imported, are being successfully produced in the country, and at this rate of progress the day is not far distant when Indian mills may be expected to meet domestic requirements both quantitatively and qualitatively.

The decline of imports from the United Kingdom and the ascendancy of Japanese goods.—The most outstanding event of the century, concerning the industry, has been the decline of imports of piece-goods from the United Kingdom, and the rise and phenomenal expansion of imports from Japan as is shown by the table below:—

Imports from the United Kingdom and Japan, and production in India, of cotton piece-goods (excluding fents):—[1]

[1] Compiled from the table at p. 27 of the *Review of the Trade of India*, 1935–36.

(*In million yards*)

Year	*United Kingdom*	*Japan*	*Mill production in India*
1905–06	2,415	—	—
1910–11	2,252	—	1,043
1911–12	2,379	1	1,136
1912–13	2,907	6	1,220
1914–15	2,354	16	1,136
1916–17	1,748	100	1,578
1918–19	851	238	1,451
1927–28	1,530	323	2,357
1929–30	1,236	562	2,419
1931–32	376	340	2,990
1932–33	586	579	3,170
1933–34	415	341	2,945
1934–35	552	374	3,397
1935–36	440	496	3,571

Between 1913–14 and 1935–36 the percentage share of Japan in the total quantities of piece-goods imported has increased from 0·3 per cent to 52·4 per cent, and that of the United Kingdom has fallen from 97·1 per cent to 46·4 per cent.

The above table also makes it clear that, in recent years, further inroad of Japanese piece-goods has been held in check. This result was, however, rendered possible only by the adoption of rather violent measures in the form of tariffs combined with bilateral trade agreements. In devising the scale of duty, it may be noted, a certain degree of preference has always been shown towards the United Kingdom.

The Mill industry *versus* the Indian cotton grower.—The making of cotton tariff in India is a delicate task of extreme complexity. India is the most important market for piece-goods from both Japan and the United Kingdom, and Japan is the biggest single market for Indian raw cotton. More than half of our exports of raw cotton, being nearly equal to the total consumption of indigenous cotton by Indian mills, goes to Japan alone. In protecting the Indian mill industry we can hardly afford to ignore Japan and thereby the interests of millions of poor Indian cultivators.

At the same time, there can be little doubt that Japan will before long develop China as a cotton-growing country. The Manchukuo Government, over which her influence is paramount, has already inaugurated a scheme for bringing 750,000 acres of land under cotton cultivation within the next twenty years. In the end the Japanese demand for our raw cotton is bound to contract, and if by that time further expansion of the Indian mill and hand-loom industries fails to absorb the surplus that cannot find an export outlet, where is the Indian cultivator to find an alternative market? At the same time, we are to avoid taking any step which may retard the development of the biggest industry of India towards its goal of self-sufficiency. It is in this background that we have to judge the negotiations that are, and that may be, carried on with Lancashire and Japan.

THE JUTE MILL INDUSTRY

Its growth.—The jute mill industry comes next to cotton in importance. The first jute mill in Dundee was established in 1838. In 1855 a beginning in spinning and weaving was made in Calcutta in earnest and a mill was erected with an output of 8 tons a day. The subsequent development of the Calcutta jute mill industry is indicated by the table below:—[1]

Year	*Sacking looms*	*Hessian looms*	*Total*
1859	—	—	192
1877	2,948	910	3,858
1890	5,359	2,300	7,659
1910	13,421	18,334	31,755
1930	22,066	36,073	58,139
1935	22,693	37,704	60,397

In addition, a number of small and medium-sized mills have recently been started, and a few more are in course of erection. There are also mills in India outside Calcutta—4 in the Madras Presidency, 3 in Bihar, and 2 in the United

[1] *The Investor's India Year-book*, 1935–36, by Messrs. Place, Siddons and Gough, p. 185.

Provinces. The total number of looms at present working in India will not be less than 66,000. It may be interesting to note that the number of looms in Dundee is only 8,500. The largest number of looms in any country outside India is in Germany where there are 11,000 looms. The total number of looms in all countries outside India is 48,955.

This industry is by far the most important manufacturing export industry of India. The value of jute manufactures exported in 1928–29, the best year of prosperity, was Rs. 56·9 crores, being 17 per cent of our total exports, as against 2 per cent in cotton manufactures which occupy the second place amongst manufactured exports. The average value of exports in the period 1879–80 to 1883–84 was only Rs. 1·2 crores. Nearly two-thirds of the jute grown is now consumed by the Indian mills.

The problem of over-production.—Due to the economic depression, coupled with internal dissension amongst the mills themselves, of late the industry is passing through a period of extreme difficulties. The problem of over-production in this industry is almost as old as the industry itself and it was to meet such a situation that the Indian Jute Mills Association was brought into being in 1884. This Association has been of great value in regulating the output of mills and making profitable working possible; but with the increase in the number of mills outside the Association the conclusion of a satisfactory agreement for the control of production is proving difficult. On the admission of the Association itself and on the basis of 54 hours' working per week, 25 per cent of the machinery in the industry is redundant. The difficulties of the industry cannot be solved by restriction of output alone unaccompanied by rationalisation and diffusion of production on new lines.

THE IRON AND STEEL INDUSTRY

The rise of a modern iron and steel industry.—The earliest attempt to make iron by European processes was made about 1830 in the South Arcot district of Madras. The

next attempt was made in Bengal in 1875 by the Bengal Iron Co. By about 1900 the average annual production of pig iron was 35,000 tons entirely from this company.

With the formation of the Tata Iron and Steel Co., and the exploitation of the enormous quantities of extremely rich iron ore deposits in the Singhbhum and Manbhum districts and the feudatory states of Mayurbhang, Bonai and Keonghar, commenced a new era in the history of the Indian industry. The first pig iron was made by the Tata Co. in 1911, and the first steel in 1913. The Indian Iron & Steel Co. started manufacturing pig iron towards 1922. At the present rate of working—nearly 2½ million tons per year—the iron ore deposits are estimated to last 1,000 years. There are likewise abundant reserves of easily workable lime stones, manganese and fluxes and other refractory materials of excellent composition.

The recent development of the industry has been in no small measure due to the grant of fiscal protection in 1924 and its continuance in some form or other thereafter. The formation of the Bengal Steel Corporation last year marks an important step forward in the development of the industry. The Mysore Iron Works are already producing steel, though on a small scale. In addition there are a number of small re-rolling mills, rolling from billets or scrap and confining themselves to a narrow range of products.

The statistical position of the industry is indicated below:—

Production (tons)

Year	*Pig iron*	*Steel ingots*	*Finished steel goods*
1913–14	218,000	—	—
1935–36	1,541,000	880,000	677,000

The position and efficiency of the industry.—The Indian industry has attained remarkable success; it produces practically all our requirements of pig iron, and exports about half a million tons every year. Further, our cost of production of pig iron is claimed to be the lowest

in the world. The domestic production of steel is now 50 per cent greater than the total import. With the incorporation of the Bengal Steel Corporation and the projected extensions to the Tata factory, the time does not appear to be far off when India will become self-sufficient in the supply of steel as well. The Chairman of the Tata Co. is reported to have declared at the annual general meeting of shareholders for 1936 that by 1940 the company would require no protection.

THE CEMENT INDUSTRY

Rapid expansion of the industry.—In spite of the large home market, and the presence of abundant raw materials, Portland cement was not manufactured in India until 1904, but the real beginning of the industry was made in 1912. Since then the industry has made phenomenal progress as is indicated by the table below:—[1]

Year	*Sales of Indian cement in India (tons)*	*Imports into India (tons)*	*Total consumption in India (tons)*
1914	945	150,530	151,475
1916	38,672	80,543	119,215
1918	84,344	20,016	104,360
1925	360,549	68,200	428,749
1930	563,929	68,000	631,929
1935–36	886,267	42,900	929,167

Early attempts towards rationalisation.—In 1924 the industry was in parlous conditions and it applied for protection. The Tariff Board declined to recommend protection on the ground that the industry was suffering from internal competition due to over-production. It found that the Indian works were already capable of producing 600,000 tons whereas the annual consumption was only 390,000 tons. Following this report, the cement companies formed a pool known as the Indian Cement Manufacturers' Association. In the following year the Concrete Association of India was

[1] *The History of the Cement Industry in India,* published by the Cement Merger in 1937.

formed with the object of educating the public in the uses of cement and providing free technical aid and advice. In 1930 was formed the Cement Marketing Co. of India Ltd., to take over control of the sales and distribution of cement. In 1936 the Associated Cement Companies Ltd. was formed to merge 10 manufacturing companies. The merger is expected to control production and effect economics in working and distribution.

Recent expansion and the danger of over-production.—The cement industry is one of the most vigorous and healthy industries of India. In a little over two decades a new industry has become firmly established, consumption has advanced from 150,475 tons to one million tons and at the same time price has been substantially reduced. Recently a number of new factories have been put up and a few more are in process of erection. In 1936–37 the manufacturing capacity of the associated companies was 1,465,000 tons. The capacity of the Dalmia group of companies (including the Rhotas factory) is estimated at another 575,000 tons, bringing the total Indian capacity to 2,040,000 tons, which is double the present consumption. Herein lies the danger, but as in the past, cheaper prices coupled with mutual co-operation, organised methods of selling and distribution, widespread propaganda and education, may enable the industry to avoid the impending catastrophe.

THE SUGAR MILL INDUSTRY

Over-rapid expansion of the industry.—Till recently, India occupied the anomalous position of being the world's second largest grower of cane, and at the same time one of the biggest importers of manufactured sugar. Within five years of the passing of the sugar protection Act of 1932, this has changed, and India is now not only self-sufficient in her requirements of sugar but a potential exporter. In 1931–32 there had been 31 factories producing 158,581 tons of sugar. In 1936–37 the number

increased to 153 with a production of 1,128,900 tons, while import of sugar fell from one million tons to below 23,000 tons only.

Attempted solutions.—Though the industry has shown remarkable growth, it has not prospered as well as it was expected to. Within five years the nightmare of over-production is staring it in the face, and it is beset with a number of very difficult problems on the agricultural, manufacturing and marketing sides. The Imperial Council of Agricultural Research and other associated bodies are doing very valuable work on some of the problems. The Government of the United Provinces and Bihar have recently passed legislation of a far-reaching character to control and stabilise the industry.

THE COAL INDUSTRY

Indian coal resources and their exploitation.—The regular mining of coal in India did not commence until 1814.[1] In the absence of any modern industry the demand for coal was very limited at this early period. With the opening up of Raniganj with Calcutta by a railway in 1854 and the advent of the factory system the coal industry made very rapid progress, as will be indicated by the figures of production given below:—

Year	*Production* (1,000 *tons*)
1846	91
1880	1,019
1900	6,118
1920	17,962
1930	23,803
1935	23,000

The coal resources of India have been variously estimated at between 36 to 54 billion tons as against 189 billions for Great Britain. In 1936 the number of Joint-Stock Coal Companies at work was 217 with a paid-up capital of more

[1] J. C. Brown, *India's Mineral Wealth*, p. 9.

than Rs. 10 crores. In addition there are a number of coal-fields owned and worked by the railways.

About 72 per cent of the total output of our coal comes from Bengal, Bihar and Orissa where the most valuable deposits of coal are found. The Raniganj and the Jharia are the two most important working coal-fields.

The problems of the industry.—Nearly 98 per cent of our production of coal is consumed in the country. The railways are the largest consumers, taking about one-third of the output, but they do not buy from the market all the coal they require as they have their own collieries. These railway collieries, often State owned, are offshoots of the high price of coal prevailing about 1921. The coal trade regards them as a menace and injustice to legitimate private enterprise.

We do not import any large quantity of coal, neither do we export much. At one time our export trade was not quite insignificant, but the wagon shortage and Government control established during the post-war boom period gave it a death-blow.

The annual *per capita* consumption of coal in India is ridiculously low. Under the auspices of the Indian Soft Coke Committee constituted in 1929, a vigorous propaganda has been started for popularising coal with encouraging results.

Mining conditions are extremely favourable in India, the seams are thick and close to the surface. Till recently both above and under ground there was an extreme lack of mechanical equipment.

Existing mining methods are very wasteful. India possesses practically unlimited reserves of second-class coal but her reserves of good quality coking coal required for the iron and steel industry will be exhausted well before the reserves of good quality non-coking coal. Hence, to avoid a possible shortage of metallurgical coal, India will have to learn to utilise to the best advantage poorer-class coals and also, as far as practicable, adopt measures for the better conservation of coking coal.

The position of India as to the factors of industrial development.—"The abundance of raw materials, the high consuming markets and the cheapness of labour," says Dr. L. Nemenyi,[1] "pre-destine India to become a highly industrialised country in the course of time." But, up to the outbreak of the last great war, the pace of industrial development in India had been very slow. The Industrial Commission mentioned various factors as being responsible for this retarded development. The natural conservativeness of the people, the inefficiency of labour, the absence of industrial and technical education, the lack of business enterprise, the shyness of capital for new undertakings, and the want of proper organisation for utilising such capital as is available are not deficiencies inherent in the Indian character, and will yield to better organisation, training and opportunity. In the words of the Indian Fiscal Commission, "education can be improved, banking facilities can be extended, technical assistance can be offered to industries." In the past the average Indian certainly showed a lack of interest in industrial development and left it to be done by the Europeans or the Parsees, but due to Swadeshi and other reasons a change has come over the spirit of the people.

Whatever detractors and interested critics might say, it is generally admitted that India does not lack in the other factors of industrial development. India is an agricultural country and must always remain so: it is natural that her leading industries are those engaged in working up agricultural products. Of the vegetable products used in manufacture, cotton, linen or jute, oil seeds, sugarcane and rubber are the most important all over the world.

Abundance and variety of raw materials and minerals: Agricultural raw materials.—India is the second largest producer of cotton in the world. Nearly 50 per cent of the production is consumed locally; the rest is exported mainly to Japan, where, after being mixed up with American or Egyptian cotton, it has built up an industry which now threatens the most advanced European manufacturers.

[1] Address to the Calcutta Rotary Club, May 10, 1938.

Indian cotton is short and coarse and will not spin yarn finer than 30 counts. In order to meet foreign competition, Indian mills find it necessary to import a certain amount of cotton mainly from Uganda and Egypt. In 1934–35, this import amounted to 4·6 lakhs of bales, being about a sixth of the total consumption of all cottons by mills. The internal production of long staple (over one inch) cotton was 51,000 bales in 1934–35 and 85,000 bales in 1935–36.[1] The importation of foreign cotton is to be deplored as India is one of the original homes of cotton and used to grow in earlier days cottons so fine as to produce the "Muslin." India suffers from no inherent defect of the soil or climate, but the cultivator has to be educated out of his indifference and conservativeness. The Sukker Barrage irrigation project opens up vast possibilities and the day may not be far off when India shall become independent of foreign supplies of long-stapled cotton.

Jute is the foundation of the second most important industry of India, and in its production India holds the world's monopoly. Though attempts have been made to grow it elsewhere, they have not so far been attempted with any measure of commercial success. About two-thirds of the crop are manufactured within India and the rest is exported.

The sugar industry—an infant of five years only—vies with the jute industry for the second position in India's industrial ranking list. The deficiencies of Indian sugar-cane and its cultivation are not inherent as is shown by the achievements of the Belapur and the Mysore Sugar Companies.

Our resources in forests are varied and vast in extent and value. They yield materials for various industrial purposes such as the manufacture of paper pulp, matches, tea chests, tool handles, etc. They also provide valuable tanning materials, certain kinds of essential oils, gums, waxes and resins. At the same time, it ought to be mentioned that a full exploitation of our forest wealth depends upon the development of transport facilities, extension of research

[1] *Review of the Trade of India*, 1935–36, pp. 175 and 228.

and experimental works and the creation of a demand by systematic publicity and organisation.

In 1935–36 we exported 43,900 tons of raw hides and skins, though vegetable tanning materials of good quality are found in most parts of India. Before the war about double the quantity used to be exported. Here again, the problem is one of capital, enterprise and organisation.

In oil seeds, India holds the unique position of being the largest producer in the world. The total area under oil seeds generally averages round 14 million acres. Almost every variety of oil seeds is cultivated and a very large proportion of the crop is exported; much of the balance is crushed by small power plants or in country bullock mills. In 1930, including native states, there were in India 289 oil factories employing 14,269 persons. In 1935–36 the value of vegetable non-essential oils exported amounted to Rs. 36 lakhs, and the value of oil seeds exported Rs. 10⅓ crores. In addition to domestic consumption, these oils constitute the basis of soaps and paints.

In 1935–36 India exported raw rubber valued at Rs. 88 lakhs and imported rubber goods worth Rs. 2 crores.

Minerals.—The mineral deposits of India are abundant and sufficient to maintain most of the "key" industries. The iron ore deposits of Orissa constitute one of the richest in quality and quantity and exist in close proximity to good coking coal. Rich deposits of lead and zinc occur in the Shan States of Burma. Copper is being successfully smelted in the Singbhum district and Burma.

The manganese ore deposits of India are probably the most extensive in the world. It is at present exported in the raw state in very large quantities. High grade chromium and bauxite deposits have been found and are being worked. South Burma is one of the richest sources of wolfram in the world. Tin is also found there and in other parts of Burma. In mica India holds the leading place in the world. The ingredients for the manufacture of good quality cement occur at many places. There are extensive deposits of medium quality coal and oil, though concentrated in

limited areas which involves high cost of transportation. This drawback in power resources is likely to be mitigated in certain areas by the development of hydro-electricity.

The foregoing analysis shows that India is favourably placed in the supply of raw materials and mineral resources. Shortcomings there are, but in most cases these are neither inherent nor insuperable. Great improvements have already been made in several directions by the application of the methods of the West and still greater progress promises to be achieved if systematic and intensive attempts are made. In the case of our mineral resources, there are no reasons to think that the position of any country is superior to ours. Further geological surveys and extension of cheap methods of transport are likely to prove helpful.

Mere presence of raw materials is not, however, a sufficient justification for the establishment of manufacturing industries in a country. Sweden sends her iron ore to Germany: United States of America sends her cotton to Lancashire. But India has advantages in the form of an immense potential internal market and an unlimited supply of cheap labour. A full discussion of the labour position will take us too far afield. Suffice it to say that, given proper supervision and suitable plant, just as accurate work can be produced in India with Indian labour as in Europe. The experiences of the Tata Iron & Steel Co., Batas, Dunlops, Braithwaites and others lend strong support to this view. Moreover, in comparing efficiencies we must not forget that Indian labour has to contend against a trying climate, less efficient management, backward factory equipment and a low standard of living. It is also necessary to remember that in India machinery is dearer and labour is cheap, while in Europe it is the reverse: hence the machine must be used to its utmost capacity even though a larger labour force has to be employed. It must, however, be admitted that India lacks the ready supply of skilled labour and scientific and technical experts who can serve as managers, foremen and entrepreneurs.

Deficiencies in capital and enterprise.—In point of capital the problem is not so much one of amount as of its shyness

for industrial employment. In spite of various official reports, nothing serious seems to have been done to produce a change for the better.

It is, however, in industrial leadership that India is most deficient. In Europe factories were established by two groups: the master craftsmen and the merchants. In India, the master-craftsmen had not the capital nor the education or the ambition to embark upon large-scale factory industry. The merchants had no experience in handling labour, and they never cared to take any responsibility for the technical side of production. Moreover, the development of trade and communications gave them ample opportunities of engaging their money. No wonder, therefore, that the early enterprises were initiated by the Europeans and a handful of Parsees. Later on, others also have entered the field, but still the position is far from what it should be.

The Managing Agency system in relation to finance and management.—Any discussion of industrial leadership and finance would be incomplete without a reference to the Managing Agency system so prevalent in India. The great merit of this much-maligned system is that it has been the natural product of the special conditions of the country and was never made to order. Of all single factors, the contribution of the Managing Agents towards the industrial development of the country has been very considerable indeed. This system in India has done what the continental system of banking did for their industrial developments. They combine command over capital with enterprise, business ability and experience. In India the rôle of the entrepreneur has been played by these Managing Agents. The idea of a venture very often originates from them, they investigate and explore, they nourish the growth of new enterprises and take the responsibility of finding the fixed and working capital in good and bad times. The system has contributed greatly to induce the flow of capital into industry. In fact, capital moves more freely into a company floated and operated by a reputed firm of Managing Agents; and it is difficult to conceive of a more satisfactory

form of industrial finance in the existing financial organisation and habits of the people. The system is a great economiser of overhead charges and should make possible considerable economies in the purchase of stores, sale of finished goods, maintenance of a highly technical staff, etc. It is also the most economical way by which scattered mills, mines, tea gardens, and miscellaneous mofussil industries can be linked up to the centres of Indian commerce, like Calcutta, Bombay, and through them to the channels of world trade. This, however, cannot be claimed of many firms of Indian Managing Agents. European firms, in spite of age, maintain their elasticity and responsiveness; but Indian firms generally confine their business to the family line and in the absence of infusion of new blood, stability and efficiency are bound to degenerate. Judged by foreign standards, the system may appear old-fashioned, but we must not overlook that in India business common-sense is undeveloped, the banking habit is a luxury of the few and the financial mechanism has been fashioned on English methods and tradition. The Managing Agency system is a peculiar Indian method to cope with a peculiar Indian situation and that is its best recommendation. We must try to devise new and better methods, but until a practicable alternative has been evolved, our problem is one of mending and not ending; and it is this which the Indian Companies (Amendment) Act, 1936, has attempted.

II. The State in Relation to Industry

The policy of *laissez-faire* and its reaction upon public opinion.— In spite of the abundance of raw materials, the immense internal market, and other fairly satisfactory conditions, our industrial achievements in the nineteenth century had not been considerable; it is only during the present century, particularly after the last war, that any remarkable progress has been made. Among other factors, one most important influence contributing to this result has been the progressive policy of the state in relation to industries. About the

close of the eighteenth century the industrial revolution was complete in England, and she had become the industrial leader of the world. She required markets for her manufactures, and quite naturally she adopted the policy of *laissez-faire*. After the assumption of direct rule by the Crown in 1858, the same policy was considered good for India even though conditions in this country were vastly different.

The consequences of this policy may well be gauged from the findings of the Famine Commission of 1880. The Commission believed that a main cause of the disastrous consequences of Indian famines was the fact that, the great mass of the people directly depended upon agriculture, and that there was no other industry from which any considerable part of the population derived their support; and they pleaded for a diversity of occupations, through which the surplus population might be drawn to manufactures. But no action was taken by the Government. Meanwhile, the Indian National Congress had come into existence, and in 1887 it passed a resolution urging upon the Government the desirability of encouraging indigenous industries and providing technical education. Since 1905 an Indian Industrial Conference has met from year to year providing a forum for the expression of the growing spirit of economic nationalism which culminated in the Swadeshi movement of 1907–08. In 1887, mainly through private efforts, the Victoria Jubilee Technical Institute was started in Bombay, and in 1904 an association was established in Calcutta for the advancement of scientific and industrial education of Indians.

The contribution of the State during this period was, in the words of the Industrial Commission (Report, para. 105), "a very imperfect provision of technical and industrial education, and the collection and dissemination of commercial and industrial information," which practically amounted to the establishment of a Commercial Museum at Calcutta, an inquiry by the "reporter on economic products" into the industrial resources of India, the founding of the *Indian Art Journal* and a series of provincial monographs on Indian industries. It is interesting to notice that

none of these concerned the organised industries, their position, prospects and possibilities. So, the conclusion is inevitable that up to the end of the nineteenth century the Government as a whole did not take any part in the modern industrial development of the country, and that if any progress was made it was in spite of the indifference of the Government.

Slight modification of Government policy towards the end of the nineteenth and the early twentieth centuries.—Towards the end of the century, however, a few individual officers adopted a more forward policy. In Madras, Mr. A. Chatterton successfully developed the aluminium hollow-ware industry, improved the hand-loom, and introduced chrome tanning of leather. In 1905, Lord Curzon set up a separate Commerce and Industry Department of the Government of India. Several Provincial Governments also now began to evince a real interest in industrial development. In the United Provinces, after the Nainital Conference of 1907, a comprehensive scheme for technical education and encouragement of industries was adopted. Loans were given, an experimental sugar factory was set up and a pioneer oil mill was started, but with little technical success and considerable financial loss. In the other Provinces also a keen interest was being taken in the revival and preservation of cottage industries and the spread of technical and industrial education. With the object of promoting the development of new industries and the improvement of existing ones, the system of State Technical Scholarships, tenable abroad, was adopted in 1903.

The forward policy of some of the Provincial Governments received an unexpected check in 1910, when Lord Morley, the then Secretary of State for India, refused to sanction the creation of a separate Department of Industries in Madras on the ground that State pioneering of industries, creation of demonstration plants, direct financial assistance and other forms of direct aid were no function of the State, and that they would interfere with private enterprise. Lord Morley's despatch naturally had a paralysing influence

upon the Provincial Governments and the Government of India, and much of what had been done had to be undone. The despatch of Lord Crewe in 1912 did not materially alter the position, though it allowed the creation of Provincial Departments of Industries.

How the last war stimulated Indian industries.—This was the position when India entered the war. The war at once demonstrated how dangerously India was dependent upon foreign countries for essential supplies; certain former imports were entirely cut off while others were reduced in volume, huge urgent purchases had to be made by the Government of India on war account, and whatever industries India had now entered upon a period of unprecedented prosperity. It was necessary to expand existing industries and to start new ones, but how could it be done if importation of machinery, technical skill and supervision, stores and other materials was not possible? It was under this stress that the Munitions Board was established, and the Industrial Commission appointed in 1916. Factories were started under the direct management of the State and many more were encouraged to come into existence with State help and patronage in various forms. Unfortunately many of these war babies succumbed on the return of normal conditions after the war.

The Industrial Commission.—The Industrial Commission in their report in 1918, made far-reaching recommendations for the active participation by the State in the industrial development of the country and for setting up the necessary administrative machinery. The main activities of the State were to include (1) research, (2) industrial and technical education, (3) commercial and industrial intelligence, (4) direct assistance: technical and financial, and (5) purchase of stores. In compliance with their recommendations separate Provincial Departments of Industries with an Imperial Department for purposes of co-ordination, were set up. On the whole, these departments have not fulfilled expectations; a number of industries were pioneered, and

loans and grants given, but the achievements were not encouraging. Better results were, however, obtained in the sphere of cottage and small-scale industries.

The policy of Discriminating Protection.—For more than a generation the Indian public had been carrying on a persistent agitation in favour of a policy of protection as a means of industrial development, but the Government dictated and controlled as it was by the British Cabinet, had consistently refused the demand, and pursued a policy of free trade. Along with other factors, the last war brought a change in this attitude; it was now realised that an industrial India would contribute to Imperial strength. The Joint Select Committee of Parliament on the Government of India Bill laid down a convention which marks the beginning of a new era. This ultimately led to the appointment of the Indian Fiscal Commission, which found that the conditions of industrial development could not be attained without stimulus in the form of protective duties. The main recommendation of the Commission, that the adoption of a policy of discriminating protection would be in the best interests of India, was accepted by the Government in 1923, and forms the basis of our present fiscal policy.

Next to tariff policy perhaps the most far-reaching measure adopted for the furtherance of Indian industries was the introduction in 1931 of the Rupee Tender Rules. In the preamble of the Rules it was announced that the Government policy was to make purchases of stores in such a way as to stimulate the development of Indian industries to the utmost extent possible consistent with economy and efficiency.[1]

[1] As an example of how the Indian Stores Department is nowadays helping the development of Indian industries may be cited the case of the Electric Bulb Manufacturing Industry in Calcutta. But for the free facilities for testing provided at the Government Test House, and helpful suggestions made by the Test House Experts, it would have been difficult for the industry to get over its initial defects and difficulties. The Stores Department gave a trial order for 10,000 bulbs—the tests continuing all the time. This order was executed so satisfactorily that the Department has now authorised the purchase of as many bulbs as the industry can supply. *Capital*, January 13, 1938, p. 56.

Government interest in cottage and small industries.—The progressive policy of the Government is manifest in other ways also. During the period of depression the Central as well as the Provincial Governments have been taking keen interest in the revival of cottage and small industries with a view to tackling the problem of unemployment and standard of living. On the recommendation of the Tariff Board in 1932, the Government of India decided to spend a substantial sum over a period of five years in reviving the hand-loom industry. The Provincial Governments also have not been lagging behind: most of them have added to the grants from the centre in promoting schemes for improvements in marketing, providing technical guidance, the supply of materials at cheap rates, etc. The small man in the silk and other industries also has not failed to get a certain amount of attention. The Governments of the United Provinces and Bengal have gone so far as to establish Industrial Corporations under Government patronage and control with a view to lending money for small-scale industrial enterprise.

INDUSTRIES UNDER PROVINCIAL AUTONOMY

The new-born zeal of the Provincial Governments to promote industries.—The newly established autonomous Provincial Governments are extremely anxious to promote by all means in their power the development of industries within their respective Provinces. The Congress election manifesto which is the basis of the programme, not only in the Provinces where the Congress is in power, but to a varying degree in the other Provinces too, contains the following as to industrial policy:—

(*a*) Encouragement of Khadi and village industries.
(*b*) Protection of larger industries, subject to rights of producers of raw materials, workers, and safeguarding of village industries.

The promptness of the Governments of Bihar and the United Provinces in passing legislation for the better

control of sugar factories, the appointment of a committee for investigating into the possibility of manufacturing power alcohol from molasses even before the publication of the report of the sugar Tariff Board, are only two out-standing instances of the new-born zeal of the Provincial Governments.

The Government of Bihar proposes to inaugurate shortly a grid electrification scheme for the expansion of tube-well irrigation on a wide scale and the promotion of industries. The idea is to generate electricity with coal distilled for the purpose. The estimated cost per K.W. of installed capacity of the Bihar scheme is expected to be lower than the cost of even the hydro-electric schemes of other Provinces.

The Government of Madras is trying to give a special impetus to hand-loom production by licensing the sale of mill cloth and introducing Khaddar for police and other uniforms. The Bombay Government in addition to hand-spinning and hand-weaving have approved several schemes for the promotion of industries. It has also established an Industrial Advisory Board to examine all new schemes and proposals relating to industrial development in the Province. The Orissa Government also is preparing an intensive scheme for the revival of cottage industries. Other Provincial Governments are not lagging far behind.

Attempts towards all-India planning.—A remarkable example of the new spirit is provided in the drive by Mr.V. V. Giri, the Madras Minister, to make India an industrially self-sufficient country. He has been making efforts to convene a conference of Ministers of Industries (as reported in the *Statesman* of June 8 and 9, 1938) from all the Congress Provinces, and from as many other non-Congress Provinces as possible, together with experts connected with basic industries, with a view to formulating a planned scheme for industrial expansion on an all-India basis.

One of the industries to be so examined will be the automobile industry. The possibilities of manufacture of locomotives for railways are also under consideration. The first scheme is likely to reach fruition soon, following talks between Mr. Giri and Sir M. Visweswaraiya at Bangalore.

The proposal is to make a start with standard cars. Foreign technicians will be engaged initially with the object of training Indians for more responsible posts so as to finally make the concern Indian-owned and Indian-managed.

Another illustration of the same spirit is provided by Dr. Syed Mahmud, Minister, Education and Development Department, Bihar, who has invited the Industries Ministers of Provincial Governments to a conference to consider the question of development of key industries in India. For the proper development of these industries he considers the following measures essential: a list of important key industries deserving State recognition and encouragement should be drawn up; the industries should be fostered in areas which are economically most suitable; indiscriminate expansion should be controlled to keep pace with demand; and currency, tariff and railway freights being vital factors, these should be adjusted to aid the progress of these industries. All Provinces and States should, therefore, present a united demand to the Central Government for help. Once it is decided to "earmark" a particular industry for a selected Province or Provinces, all other provinces should combine to help in the disposal of products and to secure other facilities (*Statesman*, June 20, 1938. Dak Edn.).

The meeting of the Congress Working Committee, held in July 1938, adopted a resolution authorising the Congress President to convene, at an early date, a Conference of Provincial Ministers of Industries. In pursuance of this resolution, the Ministers met in Delhi, early in October, under the Chairmanship of the Congress President. They agreed that the time had come when definite decisions had to be taken with regard to the starting of major, medium and cottage industries with a regular programme. A Planning Committee was accordingly appointed and is expected to take about eight to ten months to submit its report. After this an All-India National Planning Commission will be appointed, which will include not only the experts who form the present Planning Committee but also representatives of the Provinces and States willing to co-operate.

The project to make a preliminary industrial survey is both a necessary and a wise approach to the future planning of India's industrial development. It will ensure the ordered progress of industrial expansions, and help to eliminate the uneconomic competition to which many enterprises are still now exposed. The Planning Committee expects to have the co-operation of all the Provinces and some of the more important States. The Non-Congress Provinces also can by no means be said to be unmindful of the importance of developing their own industries. To the States it is an opportunity to develop their untapped resources for their own good and to find a place in the industrial structure of India. Unless the Provinces and States co-ordinate their efforts, success cannot be complete. Provincial jealousy, which has been already rearing its head in so many directions, should find no place in the evolution and working of the industrial plan.

The wisdom of the Provincial Governments themselves setting up an All-India Planning Commission may be doubted; but it cannot be helped so long as the Central Government is not democratised. It is felt that a scheme of industrial development supported by the Congress and Non-Congress Provinces and some of the States cannot fail to have a tremendous influence upon the Government of India.

As pointed out by the conference of Ministers, the ultimate object of industrial development is to solve the problem of "poverty and unemployment, of national defence and of economic regeneration in general." Hence cottage industries as well as middle-sized and large-scale industries must all find a place in such a scheme. Also there is no conflict of interest between industries and agriculture. For the soundness of our rural economy itself depends on the expansion of industries and the maintenance of a healthy balance between the two; also because the trend towards national self-sufficiency is now so well established that it might be regarded as a permanent feature of the economic structure of the future. It is no longer safe for us to depend to the same extent as before on foreign countries as outlets for our raw materials.

The solicitude of the Provincial Governments for labour.— In their anxiety to promote industries, the Provincial Governments can by no means be blamed of being oblivious of the interests of labour. In fact, it is being questioned if the pace of industrial reforms in some Provinces is not too fast. The acceptance of office by the Congress has coincided with the outbreak of labour unrest and strikes in all the important industrial centres. Further, the reports of the various Labour Enquiry Committees have made capitalists apprehensive about the future of industries in British India. These enquiry reports will serve a very useful purpose in exposing and removing long-standing injustices and inequities, but they must give a "fair deal" to the other party. If the capitalistic system is to survive at all, business activities must be conducted not for the benefit of any particular class but for the community as a whole. It is not unnatural that on the accession to political power of the wage-earning classes there should be a certain amount of effervescence, but the Provincial Governments would do well not to create any apprehension in the minds of the industrialists of any bias against them. Only by maintaining an impartial and judicious attitude will they be able to make their influence best felt and achieve the ends they have in view. The expansion and better organisation of industries which is so dear to the Provincial Governments cannot be brought about unless there is healthy co-operation between the employer and the employed. And to this end the time seems to be ripe for the establishment of an Industrial Council as suggested by the Whitley Commission. Indian labour is fully alive to its strength, and the use and potentialities of the strike; it, however, remains untrained in the art of negotiation and lacks the organisation and leadership so essential to the welfare of industry as a whole. The truth of this statement will be amply borne out even by a superficial examination of the history of any one of the large crop of major industrial disputes of the past and the present. It is urgently necessary for labour, and those who are interested in industrial development, and have the privilege and power to mould

policy and practice, to realise that capital and labour are mutual trustees and that both are the trustees of consumers.

III. Conclusion

The extent of industrial development and the danger of over-production in certain lines.—The Indian Industrial Commission, after a very searching inquiry, summed up the industrial position of India in the following words[1]:—

"The industrial system is unevenly, and in most cases inadequately, developed, and the capitalists of the country, with a few notable exceptions, have till now left to other nations the work and profit of manufacturing her valuable raw materials, or have allowed them to remain unutilised."

The Indian Fiscal Commission not only endorsed the findings of the Indian Industrial Commission, but went further to say that "the industrial development of India has not been commensurate with the size of the country, its population, and its natural resources."[2] They summed up the then industrial position as follows:—

"We find in the cotton and jute mills two important industries of modern type, a considerable diffusion of mechanical engineering represented by the railway work shops and the private engineering works which are now springing up, the beginnings of an iron and steel industry, and a number of minor industries, none of which has yet reached a stage of being a serious economic factor in the country. In addition there is a large production of mineral oil, and there is the important industry of coal mining, on the future of which the industrial development of the country largely depends."

Since then, in a decade and a half, there has been phenomenal progress in certain industries. India now produces about 80 per cent of her requirements of cotton textiles; in five years she has become self-sufficient in sugar; cement was produced for the first time in 1914 and now foreign cement has almost been eliminated; further, the

[1] *Report of the Indian Industrial Commission*, p. 243.
[2] *Report, Indian Fiscal Commission*, p. 23.

consumption of cement has increased while its price has been substantially reduced. In the protected varieties of paper India is nearly self-contained; by 1940, when the projected steel works at Hirapur commence operation, India will hardly need any foreign steel. In matches she is already self-sufficient. India has two manufacturing export industries—jute and pig iron. The jute industry is in a serious plight partly on account of an undue expansion of productive capacity; and the foreign market for our surplus pig iron is extremely precarious and uncertain. The utmost that Indian industries can aim at, consistent with safety and stability, in their present stage of development is national self-sufficiency and that stage is being reached fast in some at least. In fact, over-production threatens three of our industries, *viz.*, jute, sugar and cement, and the immediate problem in them is one of consolidation and rationalisation rather than any further expansion of productive capacity.

In addition to these major industries, a wide variety of minor industries have also been started—some of which are fairly well established, but the majority are still struggling hard to take root in the industrial system of the country.

Drawbacks of our industrial developments.—Notwithstanding the substantial progress of recent years, the extent and stage of industrial development in India is far from satisfactory. Even after a century of industrialisation there are 9,261 large industrial establishments employing 1,840,792 persons, *i.e.*, only one in every two hundred of the population. The commodities produced by these factories meet only a fraction of the total requirements of the people and make a poor show by the side of the great volume and variety of goods imported from abroad. This is particularly regrettable in view of the abundance and wide range of raw materials which are available but exported and then received back as finished goods. Our major industries have very largely expanded their productive capacity, but most of them are of a basic and rudimentary character. The two foremost industries of India, *viz.*, jute and cotton, are engaged in working up

agricultural raw materials into simple manufactures: production of higher counts of yarn, the finest quality of piece-goods, jute canvas for shoes and other purposes, jute carpets and a variety of other goods in which jute is mixed up with other fibres or materials have not yet been seriously taken up in this country. We have a considerable iron and steel industry, but railway plant and rolling stock, machinery of all descriptions and many other types of metal manufactures are almost exclusively obtained by importation.

We are still engrossed with the problems of our coal, cotton, iron, steel and other basic industries, while the progressive countries of the world are trying to redress the balance of the old by developing the modern industries of electricity supply, the manufacture of radio and electrical equipment, aluminium, rayon, synthetic dyestuffs, foodstuffs, oil extraction from coal, air and motor transport, film production and cinema display. Although we are almost self-sufficient in the supply of cement, matches, sugar, pig-iron, and have lately made remarkable progress in the production of cotton piece-goods, steel and paper, we are still in the primitive stage of industrial development, and our dependence upon foreign countries for a thousand and one other manufactures is ridiculously sublime—particularly in the case of factory equipments, power plants, stores, replacement parts, etc. The chemical and engineering industries are universally recognised to be the starting point in modern industrial development, but in India we have hardly yet made a beginning in these directions.

There are a number of accessory industries, workshops, gins and presses, rice and timber mills, but complex industries requiring the employment of complicated machinery and processes, and involving technical guidance of an intricate and specialised character, and utilising by-products are absent. Certain recent innovations like the Bata Shoe Factory, the soap factories of Lever Brothers, the Dunlop Rubber Factory, the Western India Match Co., and the projected chemical works of the Alkali and Chemical Corporation[1] are all monumental reproaches to the Indian.

[1] These cases of foreign companies starting factories in India under

Indian enterprise and capital are shy of developing on new, untried lines. We prefer to imitate rather than initiate. The potential productive capacity of the Cement Merger is greater than the present consumption, the production of the protected varieties of paper is nearly equal to its present consumption, and yet we have recently witnessed the flotation of a number of cement and paper companies.

We have no research departments attached to our industries.[2] When a new and better process has been invented and tested to satisfaction in the West, we come forward to adopt it, but by that time it has probably gone out of date in its place of birth, and been replaced by a still better technique.

Judged by Western standards, our industrial achievements, however creditable in themselves, must be regarded as being extremely poor in quality and quantity. Even after 75 years of development, though there is no lack of raw materials and market, India is a baby in arms in industrial production. In fact industrialisation is only beginning in India and the present state of her industry can hardly be compared with that of England or Germany or America. It has not yet divorced the factory workers altogether from the land, nor produced the great agglomera-

the shelter of protection with an Indian name and with a sprinkling of Indian directors on the Board raises a difficult question to which an answer is urgently called for. The object of a protective tariff in every country is to benefit the country and its nationals by industrial development. Can it be claimed that this spirit behind the tariff is being fulfilled by the Bata and Dunlop factories ? The External Capital Committee in para. 20 of their report raised this question and did not hesitate to give a clear lead. They rightly pointed out an inconsistency in the position of the Fiscal Commission in this respect and concluded by saying that some form of control is desirable. Public opinion, as reflected by the Congress Working Committee, has not failed to record its disapproval of the new form of invasion. In fairness, it may not be hard to admit that industrial development of the type launched by Batas, Lever Brothers, Dunlop and the like could not be initiated by Indians with equal promise and that it would entail a huge capital expenditure, a long period of experiment and unavoidable reverses. One might cite the example of the Tatas in relation to iron and steel, but Tatas are born and not made. Should we wait till another Tata is born or should we make the best of a bad bargain with the Batas and the host of them ?

[2] The jute industry has made an innovation in this respect but very recently.

The responsibility for research in cane and sugar has practically been taken by the Government.

tion of wage-earners in cities so characteristic of industrial life. In consequence, industrial organisation is more difficult both for the employer and the worker, for the employer because he cannot count on a highly trained and largely permanent labour force wedded to industry, for the worker because collective action for improving his conditions of employment and standard of living is much harder to organise. There is also lacking the same desire for higher standard as in the West. But this is not to be wondered at; in the early stages of industrial development, it is bound to exist, until people have tested the advantages of better living. The taste, however, comes rapidly when it is encouraged. It is also true that people in India cannot work with the same intensity as in temperate climates; the speed of production as well will never quite equal that of the West. There are many other features which distinguish Indian and Western conditions, at any rate in their present stages. But for all that it still seems that the general lines of development are at bottom the same.

The example of Japan.—Another eastern country, namely Japan, however, has done wonders in a shorter period and in far less favourable conditions. The immense quantity of goods she is pouring into the markets of the world, and particularly the low prices at which they are sold, are really shocking to her competitors. An important contributory cause of this was the depreciation of the yen by more than 40 per cent of its previous value, but another more permanent factor was the pressure of a large agricultural population with little room for expansion which kept down industrial wages and labour costs. The same situation exists in India, but with a different result. There is no reason why Indian industries should not approach the Japanese standard of efficiency, given capital, organisation, education and State aid.

Time is ripe for the appointment of an Industrial Commission.—To take stock of our industrial position as well as to suggest lines for future development, the time seems to us to be ripe for the appointment of an Industrial Commission.

Those industries which enjoy tariff protection may have their position examined periodically by the Tariff Board, but a Tariff Board inquires into an industry piece-meal cut off from its proper setting in the industrial system of the country. The task of such a Commission will be to take a comprehensive view of the whole system, to investigate into new lines which Indian industry can embark upon, to suggest measures for the consolidation and rationalisation of those industries in which over-production is threatened, to dovetail the policies and actions of the various Provincial Governments with each other and with those of the Central Government, to find the rightful place for handicrafts and minor industries in the Indian scheme of industrial organisation, to reconcile the contending interests of labour, capital and consumer and to investigate into other allied problems. The Commission will also go into the question of the advisability of attaching permanent Advisory Committees to Provincial and Central Departments of Industries.

During the last twenty years India has undergone rapid political and economic evolution. For good or evil, but as it seems to us quite inevitably, India is adopting the economic organisation of the West. The idea that a country should as far as possible produce what its people need is taking root in this country as well as Europe, despite all the teachings of Adam Smith and his disciples about the advantages of international division of labour. This tendency towards greater self-sufficiency is one of the outstanding features of economic development during the twentieth century. The spread of education, the advance of technique and the expansion of liquid capital produced conditions in which every country decided to develop its basic industries as far as raw materials, labour and a consuming home market were available. The last Great War gave a tremendous impetus in the same direction. It is useless to condemn it. Also it is necessary to realise that, as in many other matters, India can be no exception to this trend of world economic evolution, particularly because India possesses a superabundance of raw materials, vast domestic consuming markets and cheap labour. What we have to do is to recon-

struct the economic system of the country on a basis in which nationalistic policies must somehow be incorporated.

It is in this light that the recent industrial policies and programmes of the Provincial Governments should be judged. To develop industries to the stage of self-sufficiency from a pin to a steamer has always been, and is, the cherished ambition of the average Indian. Provincial autonomy has given the chance, and quite naturally the various Governments are trying to bring about an industrial Millennium. After generations of governmental callousness, inactivity and open or veiled hostility, the present overflow of enthusiasm is not difficult to understand. But it must not be forgotten that State policy, though an important consideration, is not the only or the sole factor in industrial development. Subject to this qualification, the enthusiasm of the Provincial Governments is thrice welcome. There is unlimited scope for their activity in the fields of research, finance, marketing, etc., but in pursuing these aims care should be taken to avoid certain pitfalls. A healthy and vigorous industry cannot grow tied to the apron-strings of Government. The anxiety to promote industry may give rise to a sort of rivalry which may degenerate into extreme provincialism. Again, in encouraging small industries any conflict with big or organised industries should be avoided; in India there is enough room for both. Further, there should be perfect understanding and co-ordination of the Provinces between themselves and with the Government of India.[1] Development of industries may require not only the shelter of a protective tariff, but also the indirect support of a suitable exchange, currency, railway freight and kindred policies. The powers of the Provincial Governments in these spheres are after all limited, and they are helpless unless they can carry the Central Government along with themselves.

[1] The necessity for such co-ordination is amply illustrated by recent events. Sugar control legislation passed in two Provinces may drive the industry to other Provinces and Indian States and thus defeat its purpose in the end. It also raised the constitutional question of the power of the Provincial Governments to tax sugar. Similarly, if effect is given to the reports of the Bombay and Cawnpore Textile Labour Inquiry Committees regarding increase of wages and other matters, it must inevitably have repercussions upon other textile centres, and thus in turn raise the question of co-ordination of Provincial policy in matters relating to labour.

CHAPTER XX

MINERAL RESOURCES AND INDUSTRIES

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In approaching the various problems concerning India's mineral industries one is faced with either of two difficulties. On the one hand there is the tradition that India is a land full to overflowing with valuable minerals, many of which have enriched her own people or merchants and others from other countries for centuries in the past. On the other hand we have the cry that the country is far too dependent upon other countries for commodities of all sorts and that every effort should be made to utilise to a greater extent the minerals already used in her industries, or exported, and also to search for and utilise to the fullest extent possible the hitherto undiscovered mineral resources and so render India as far as possible independent of other countries in the world.

The illusion of the traditional picture is the more difficult to dispel, at least among peoples of Western countries, who forget, or never properly realise, that India is not a country but a continent, with as many climates and varieties of geological and topographical structure as, say, the continent of Europe and with as many varieties (both actual and potential) of occupations and industries too.

A study of India's mineral resources and of the problems of its mineral industries must necessarily be largely statistical and comparative. The space at our disposal is insufficient for more than a mere cursory glance at the whole picture, attention being directed to specially interesting details here and there. In compiling the information that follows, an

attempt has been made to bring into prominence those facts that speak for themselves. The student of economics should have no difficulty in seeing the directions in which further research is likely to repay the time spent on it.

The Geological Survey of India, the one important source of up-to-date information concerning the mineral resources of India, classifies the minerals of the country into two groups, namely:—

(*a*) those regarding which statistical information is more or less complete and reliable, and
(*b*) those regarding which the information is incomplete or almost lacking.

The student of economics requires information more readily accessible. Accordingly the minerals are here treated in alphabetical order.

Before attempting a systematic study of the minerals in alphabetical order, however, the following reference to their relative economic importance will be of value.

RELATIVE IMPORTANCE OF MINERALS

The minerals of greatest importance, measured in terms of annual value of output, are the following, in the order given, the approximate sterling value of the output for 1933 (for minerals of annual output of £100,000 and over) being stated within brackets:—

Petroleum (£4,708,000), coal (£4,600,500), gold (£2,078,200), salt (£859,000), lead and lead ore (£851,300), building materials (£800,000), tin ore (£533,100), silver (£497,200), copper ore (£392,250), mica (£307,650), zinc concentrates (£231,800), iron ore (£187,800), manganese ore (£123,150), nitre or saltpetre (£117,150), tungsten ore, nickel speiss, ilmenite, antimonial lead, chromite, clays, steatite, jadeite, refractory materials, magnesite, ruby sapphire and spinel, fuller's earth, monazite, gypsum,

diamonds, ochre, barytes, zircon, beryl, felspar, bauxite, garnet, apatite, bismuth.

The order of economic value of a mineral varies, however, from year to year, on account of fluctuations, sometimes of such major importance as to cause food for serious thought for the economist and anxiety for both industry and Government. If the above list is compared with the corresponding list for 1932 it will be found that the production of petroleum had increased in 1933 by barely 25 per cent, coal having lost first place partly on that account and partly on account of a 10 per cent fall in output.

The output of gold increased by 10 per cent. Not only so, but great quantities of hoarded gold exported in the last few years have raised the export figures to values totally out of proportion to the normal. The output of gold more than doubled between 1932 and 1933 and that of antimonial lead almost trebled. The output of manganese fell by over 36 per cent—a matter of the greatest concern to the industry. The output of tin ore increased by over 50 per cent, and so on.

The economist who wishes to study the mineral industries of India has an exceedingly interesting, but difficult and extensive, task before him, each important mineral requiring exhaustive consideration of statistics relating to a long period of years as well as of industrial and political events of peculiar significance and importance, especially those of very recent years.

In the list that follows there will be found a concise statement of the important sources of the various minerals, a note regarding annual output, and, as already stated, a brief reference to any specially interesting point that appears to be worthy of mention, such as disproportionate amounts of imports in the face of large resources, important uses, etc.

INDUSTRY'S SHORTCOMINGS

The student of economics will be impressed, on consulting the literature, by the references to the shortcomings of

suppliers of minerals and their derivatives in this country. Both European and Indian firms would appear to be blameworthy in this respect.

In spite of the spread of technical and scientific education in recent decades there frequently is a regrettable failure to apply scientific and even business principles in a practical manner and, whatever is to blame for it, whether climate or not, even imported talent frequently deteriorates in the same direction. A whole industry may suffer and almost collapse, as did the coal industry in the early post-war years, through causes traceable in large measure to this defect.

In the list that follows there occur many minerals that are extensively found throughout India but are at present little used. Their exploitation requires in many instances the highest degree of scientific training and technical experience. The student of Indian problems is cautioned against working up unjustifiable optimism or even undue enthusiasm over India's mineral resources. Mere possession of mineral wealth provides no short cut to industrial prosperity.

EFFECT OF RAILWAY FREIGHTS

There is one stumbling-block that has to be removed by the heavy industries in India, and that is the crippling effects of railway freights. India is such a vast continent that great distances have to be traversed by mineral products before they can be used in manufacture. Coal is a striking example of this (see COAL) and of course the vast majority of mineral products require cheap coal for their conversion into marketable commodities or even for their transport to internal markets, quite apart from the export market. If the minerals in question are found at a great distance from the coalfields this same adverse effect operates. The difficulty is increased in India by the fact that most of the coal of the country is more or less localised. If there had been several important coalfields throughout the country the story would have been quite a different one.

This does not necessarily mean that railway freights are unfairly high in India. A case *might* be made out for such a contention, or as an alternative the economist might make out an excellent case for special discriminating freights on certain commodities, or on such commodities when conveyed to certain destinations, or in respect of certain minimum distances, which freights could not by themselves be considered but which, on account of possible improved internal trade and increased exports, might be more than justified.

LARGE IMPORTS IN SPITE OF RESOURCES OF RAW MATERIALS

Undoubtedly the most interesting feature of India's mineral industries at the present day is the inability of the country to manufacture all of those domestic requirements for which she has the bulk of the raw materials. A glance at the figures regarding imports of manufactured articles made almost entirely from minerals gives point to this remark. An average quantity of well over Rs. 36,00,00,000 worth of such materials is annually imported Outstanding among these are machinery, mill-work plant, railway plant, rolling stock, cutlery and hardware. These alone account for Rs. 29,00,00,000. The predominance of imports of what are mainly iron and steel articles is striking.

Glass and glassware imports amount to over Rs. 2,50,00,000 and dyestuffs to over Rs. 2,00,00,000. It is doubtful whether India could for many years compete in the manufacture of the latter, but there seems little reason to doubt her ability to make most of her own glassware. Her iron and steel industry has for many years shown that time is the only factor required to place it on a satisfactory footing in the matter of independence.

Of less importance in this study is the question of reserves, except perhaps in respect of deposits of petroleum. In spite of (perhaps partly because of) an army of experts, no one can authoritatively state what reserves there are of any mineral in the world, and estimates alter from decade to decade in such a manner as to render almost futile a

close study of most of such figures. India's reserves of coal as at present calculated will probably last her for two or three hundred years. Her reserves of iron may be confidently expected to do the same.

Quantities referred to below generally relate to annual production.

Abrasives.—*Corundum or Emery* occurs throughout India. Certain varieties are well-known gemstones. Many artificial products are now on the market (*e.g.*, carborundum, hard steels, alundum, etc.) and little chance industry developing. Occurrences: Salem (Madras); Hunsur (Mysore); Pipra Rewa State). 10 tons to 60 tons (Rs. 1,000 to Rs. 5,000). *Garnet* another important abrasive: Ajmer; Tinnevelly (Madras); locality between Afghanistan and Chitral. Up to 1,000 tons (480 in 1928) from Tinnevelly.

Alum and Aluminous Sulphates.—(Does not include aluminium, for which see BAUXITE.) No workable deposits. Former manufacture of alum from pyritic shales almost extinct. Almost entire output from Mianwali (Punjab): 6,000 cwts. (Rs. 1,00,000), 1922; 478 cwts. (Rs. 8,000), 1928; none since. 60,000 cwts. (Rs. 4,00,000) ann. imports alum and similar compounds. Used in tanning, dyeing, water softening and pharmacy. Import duty 25 per cent *ad valorum* or Re 1/6 per ton (whichever is the higher).

Aluminium.—See BAUXITE.

Ammonium Sulphate.—See COAL.

Antimony.—Formerly mined various localities but only now from Amherst dist., Burma. 500 tons (Rs. 10,500), 1927; 370 tons (Rs. 10,300), 1928; 3 tons (Rs. 60), 1930; none since. Antimonial lead (contains lead, antimony and silver) exported by Burma Corpn. to U.S. Over 1,000 tons (Rs. 3,20,500), 1926; almost 1,500 tons (Rs. 2,40,000), 1933.

Antimony largely used in form of alloys, *e.g.*, type metal. Compounds used in pharmacy; manufacture of pigments,

matches, fireworks, etc. Antimonial lead used for lead plate accumulators.

Arsenic.—Extensive deposits orpiment and realgar Chitral. Arseno-pyrite near Darjeeling and Bhutna valley (Kashmir). Orpiment in Kumaon. Av. ann. export arsenic 6 tons (Rs. 5,000). Ann. import 80 tons (Rs. 1,00,000) of which 10 tons re-exported. Arsenic compounds important in many industries. Orpiment and realgar are important natural pigments. Ann. imports up to 9,000 cwts. (Rs. 2,15,500).

Asbestos.—Good long-fibre deposits rare but occasionally found, and valuable. 20 tons (Rs. 1,876) from Bhandra dist. (C.P.) recently; 40–150 tons per ann. from Seraikela State (B. and O.), 90 tons (Rs. 9,000), 1932. Cuddapah and Ajmer-Merwara also important. Production for India nearly 320 tons (Rs. 16,160), 1929; 33 tons (Rs. 1,190), 1930.

Asbestos extensively used as lining for electric furnaces, fireproofing purposes and as heat insulator.

Barytes. Akwar State (Rajputana); Betamcherla, Anantapur and Cuddapah (Madras). 2,303 tons (Rs. 31,341), 1924; 5,651 tons (Rs. 41,517), 1932. Mineral of rapidly increasing importance, used in paint industry, as filler for paper, india-rubber, etc., and in pharmacy. Large ann. imports: 9,400 cwts. (Rs. 40,000), to nearly 1,700 tons (Rs. 1,37,000).

Basic Slag.—See IRON AND STEEL and PHOSPHATES.

Bauxite.—Only source of metal aluminium at present but in spite of extensive good quality deposits no present production of metal. Aluminium manufactured by elaborate electro-chemical process requiring enormous amounts cheap electric current. Reliable supplies mineral cryolite also essential. Production nearly 4,500 tons (Rs. 8,300), 1932. Approx. 70 per cent of world's ann. requirements bauxite (1,500,000 tons) used for production aluminium; remainder for manufacture of abrasives, chemicals, refractories, cements, etc. Enormous potential industry even for latter

substances awaits development in India. Nearly 70 tons aluminium imported 1933.

Bismuth.—Small quantity bismuth minerals obtained as by-product during treatment wolfram and tin deposits Burma. (See TIN.)

Borax.—No occurrences known in India. Ann. imports from Ladakh and Tibet, and other countries (over 1,000 tons 1933), increasing.

Building Materials.—Complete statistics not available. Large variety natural rocks used locally all over India. Transport expense generally limits use to localities of occurrence. At Calcutta, Bombay, Madras, etc., foreign stones, *e.g.*, Italian marble, Scotch granite, extensively used for flooring and ornamental purposes, though similar material available in India. Enormous quantities of the following used: igneous rocks of Charnockite series of Madras; gneissose granites of Mysore; slates and limestones of Central India, C.P. and U.P.; Gondwana sandstones of Bengal, Bihar and C.P.; coralline limestones of Narbada valley; nummulitic limestones of north-west; Porbandar stone of Kathiawar and innumerable ornamental stones.

In addition large quantity materials mined and quarried for manufacture of cement (q.v.) and bricks. (See CLAY.) In spite of large quantity available, enormous quantities annually imported: Rs. 1,11,00,000 building materials, including bricks, tiles, asphalt, cement, etc. See CEMENT.

Annual production over 1 million tons granite and gneiss (Rs. 20,000,000) for building and road metal. Bulk of this in Rangoon for railway development and town reclamation work. About 400,000 tons (Rs. 10,50,000) sandstone annually quarried in B. and O., Burma, Rajputana, etc. Limestone extensively used for building, manufacture of cement and as flux in iron and steelworks. 2,750,000 tons (Rs. 48,00,000), to over 3,000,000 tons (Rs. 52,00,000) limestone quarried annually (includes 20,000 tons to 300,000 tons dolomite). Some hard forms laterite used for building and road metal. Statistics unreliable but annual production probably from

300,000 tons (Rs. 3,50,000) to 700,000 tons (Rs. 6,85,000). Slate also important material, found Kangra dist.; Gutgaon dist. (S. of Delhi); Kharakhpur hills (Monghyr dist., B. and O.). Annual production: 12,000 tons to 19,000 tons (Rs. 1,80,000). Used also for electrical switchboards. Stone for road metal is not liable to import duty. Other stones and marble subject to 15 per cent *ad valorem*.

Cement.—Nearly Rs. 7,00,00,000 industry firmly established since Great War. Annual production. Portland Cement under 100,000 tons before 1920; now well over 500,000 tons. But annual imports over Rs. 50,00,000. Import duty formerly Rs. 9 per ton (Portland cement) or 15 per cent *ad valorem* (other cements including white Portland cement) now Rs. 18/4 and 30 per cent respectively (20 per cent *ad valorem* if from U.K.). Some Indian limestones fortunately contain all chemical elements, and those in nearly correct proportions, necessary to make high grade Portland cement, without other ingredients. Others require addition clayey material and even gypsum during processes involved. Complete list localities of manufacture impossible in space available. Following specially important: Katni (C.P.); Dwarka (Kathiawar); Japla (Daltonganj); Banmor (Gwalior); and Shahabad (Hyderabad State). Chemical composition all cement-making materials extremely important. Rapid setting cements, containing high proportion alumina, manufactured (not in India) from bauxite and limestone. Possibility considerable extension cement industry in India on account of great natural resources of both those minerals.

Chromite.—Source of metal chromium and its compounds; also a refractory. Found in Baluchistan, Mysore, Singhbhum, Andaman Islands and Salem (Madras). Annual production 35,000 tons to 60,000 tons, falling recently; 15,500 tons (Rs. 2,23,000), 1933. Except for small quantities used for manufacture of firebricks, bulk is exported. Compounds used in chemical industries and for tanning and chromium plating.

Clays.—Statistics of clay and allied industries are valuable index of industrial life of a country. Reliable Indian

statistics not available, partly owing to widespread village industry. Large quantities fireclay for manufacture of firebricks, and other refractory materials obtained in B. and O., especially the coalfields. China clay for manufacture of fine pottery and earthenware obtained in B. and O.; Jubbulpore (C.P.); Burma; Mysore; Madras and Delhi. Fuller's earth mined Mysore; Rajputana; C.P. Recent annual output by organised industry over 200,000 tons clay (Rs. 2,50,000), plus 25,000 tons China clay (over Rs. 1,00,000). Annual imports, however, over 26,000 tons China clay (Rs. 20,00,000) mainly from Cornwall, England. Well over Rs. 1,00,00,000 manufactures: pottery, earthenware, china, etc., and clay imported annually. Clay other than China clay subject to import duty of 25 per cent *ad valorem*.

Important field for manufacture of glazed pottery, incl. sanitary ware, insulators, scientific apparatus, etc.

Coal.—Vast reserves of coal, estimated at over 50,000,000,000 of tons, including coal suitable for manufacture of good quality metallurgical, (*i.e.* "hard") coke. Mostly relatively high ash but comparing favourably with coals from S. Afr., Japan and U.S. Bengal and B. and O. coalfields' output overshadows all others but adjoining C.P. field is of increasing importance. Recent annual production over 22,000,000 tons, of which over 90 per cent from Bengal and B. and O. Over 1,600,000 tons converted into hard coke. From 12,000 to 21,000 tons coke imported.

Hyderabad production about 3 per cent of total; coal friable and rather poor quality. Assam and Punjab coals sometimes of very low ash but much sulphur. Bengal, B. and O. and C.P. coals have little sulphur. Much very friable lignite in Kashmir and Bikaner.

A recent development is the soft coke industry to provide comparatively smokeless domestic fuel—an effort to utilise low-grade coal and discourage waste of cow dung (fertiliser). Industry growing partly owing to intensive sales propaganda, partly to research into scientific methods of manufacture, both financed by Indian Soft Coke Cess Committee. Coal distillation by-product industry relatively less import-

ant than in more highly industrialised countries, partly due to competitive price of imported ammonium sulphate, of which nearly 35,000 tons imported 1933, whereas only 10,000 tons made. Important industry is the production of coal tar for road-making, manufacture of paints, phenols, etc.

Recently much competition from coal imported from Britain, S. Afr., Portug. E. Afr., Australia, and Japan. S. Afr. and Jap. coals competing mainly on account of price cutting, but partly due to heavy inland freights, which inevitably hamper industry, raising price per ton from a few rupees to Rs. 15 or Rs. 20. Industry suffered after Great War largely due to improper attention to maintain quality. Between 1924 and 1925 export trade almost disappeared. Confidence restored and imports risen since establishment of Coal Grading Board (1925), and exports rose to over 2,000,000 tons, but world depression caused exports to fall to under 500,000 tons (Rs. 41,00,000), 1933. Exports mainly to Ceylon (200,000 tons), Hong Kong, U.K., Straits Settlements and Philippine Is. Coal, coke and patent fuel liable to import duty of 10 as. per ton. Coal tar and pitch, to an import duty of 25 per cent *ad valorem*.

Many interesting problems, economic and otherwise, worth investigation. Great difficulties in way of scientific development of industry, research, etc., which require funds that financial state of industry does not at present appear to justify. Co-operation in matter of pumping, selling, etc., which might greatly help industry apparently impossible of achievement without intervention of Govt. Inland market would appear to offer some hope of expansion but not in near future. In this connection note large imports of fuel oil which is replacing coal or being used where coal might be used if conditions otherwise favourable. (See PETROLEUM.)

Cobalt.—Occurs Khetri, etc. (Rajputana). (Also rich deposits Nepal.) Cobalt and nickel present in small quant. in manganese ores. 3 per cent to 4 per cent cobalt in nickel speiss from Burma. (See NICKEL.) Khetri ores used for production of blue enamel.

Copper.—After several decades of alternating slight prosperity and complete disaster industry now established and progressing by careful and capable exploiting of natural resources. Occurrences: Singhbhum (B. and O.) and surrounding country; and to a less extent various places in South India, Rajputana and along outer Himalayas. Also occurs in Burma Corp'n. mines, and much copper matte obtained during treatment of ores. (See LEAD.) Only important deposits worked are those of Indian Copper Corp'n. near Ghatsila (Singhbhum). Annual production of ore, containing about 3 per cent copper, 30,000 tons, 1928; 76,800 tons, 1929; over 200,000 tons (Rs. 22,13,000), 1933. Copper matte from Burma, 10,000 tons (Rs. 20,00,000) to 12,500 tons (Rs. 30,00,000). Almost unlimited field for utilisation of copper in India, especially for bazaar and other requirements in brass for domestic utensils, brass and bronze castings for engineering purposes, etc., and for electrical purposes. No electrolytic copper (essential for last-mentioned) made in India but when made in future, imports of electrolytic copper will presumably disappear and nickel present in Singhbhum ores may be recovered.

Diamonds.—Indian output insignificant. Found mainly in three areas: dists. of Cuddapah, Anantapur, Bellart, Karnul, Kistna and Godaveri; Mahanadi Valley, *e.g.*, Sambalpur and Chunda; country around Panna, *e.g.*, States of Panna, Charkhari, Bijawar, Ajaigarh, Hothi, Pathar, Kachhar, Baraunda and Chobepur. Accurate statistics not available. Recently 200 carats (Rs. 36,000) to over 1,250 carats (Rs. 72,000), produced in States of Central India; 2,342 carats (Rs. 63,695), 1933.

Dolomite.—See REFRACTORIES.

Fireclay.—See CLAYS.

Fluor Spar.—Useful flux, and source of element fluorine and of fluorides. Small quantities found extensively, *e.g.*, Barla (Kishangarh State); Sleemanabad (Jubbulpore); Drug (Rewa State). Barla deposits most important. High cost

of freight prevents working at present. Bengal and B. and O. annually import 500 tons to 2,000 tons for iron and steel industries.

Gemstones and Semi-Precious Stones.—Difficult to apply proper perspective to this group of minerals. Statistics not available owing to widespread nature of industry, methods of leasing mining rights, etc. Practically any pretty stone may be regarded as precious. DIAMOND and RUBY, SAPPHIRE and SPINEL treated separately (the last three under "RUBY"). Only very brief notes follow as volume of trade does not justify more. Agate, carnelian, cat's eye, etc., rock crystal, rose quartz, amethyst, etc., opal, found in rivers draining Deccan trap. Rajpipla specially famous for agates. Amber found at Myitkyina and Upper Chindwin (Upper Burma). Beryl, aquamarine, etc., found in chief mica districts in B. and O.; Nellore; Ajmer-Merwara; Scardu (Kashmir), etc. Beryl is also source of metal beryllium. (See RARE MINERALS.) Garnet rarely good enough to be precious. Large quantities mined for abrasive (q.v.). Tourmaline found in Ruby Mine dist., Upper Burma.

Glass-Making Materials.—Glass-making is a rapidly growing industry in India. Good quality sand is a most important raw material. Occurrences: Mangal Hat and Patraghatta (Rajmahal Hills); Loghra and Borgorh (near Allahabad); Sankhada and the river at Pedhamli (Baroda); Jubbulpore (C.P.); and many other places. Some usable deposits are sands, some sandstones, some quartzite rock, etc. etc. Another important ingredient is soda, as soda ash or salt cake. Bulk of soda ash is imported. Lime is also used. (See CEMENT and BUILDING MATERIALS.) Saltpetre (which supplies potash) is sometimes important. (See SALTPETRE.) Enormous quantities glass and glassware imported, *e.g.*, over Rs. 2,50,00,000 per annum. Japan, Czechoslovakia, Germany, U.K., Belgium are most important sources. Bangles and beads account for Rs. 1,00,00,000 to Rs. 1,40,00,000 of imports; bottles and sheet and plate glass for Rs. 30,00,000. Extent of potential industry may be gauged from above figures. Minor but

important ingredients for making special coloured or optical glasses are also found in India. Note that for making some special glasses and for making the articles from them, a very high degree of technical skill and many years' experience are required.

Gold.—Out of 20,000,000 oz. gold produced in the world annually India produces about one-third of a million ounces (about 2 per cent of total), and is eighth among world's producers. Over 99 per cent of India's gold comes from Kolar gold field (Mysore). Small quantities from Madras, Kashmir, Punjab, U.P., and Singhbhum (B. and O.). Annual production, 330,500 oz., 1931; 329,700 oz., 1932; 336,100 oz. (Rs. 2,76,40,000), 1933. Kolar field noted for great depths reached in mines (over 7,400 ft.) with high temperatures (up to 130° F.) and great danger due to rockbursts. An important associated industry is production of electric power (for the mines) at the Cauvery Falls, over 92 miles away.

Graphite.—Occurrence sporadic throughout India, *e.g.* Vizagapatam hill-tracts, Orissa Feudatory States, Chota Nagpur (Bihar), Goorg, Godaveri Dist., Upper Burma, Travancore, Sikkim. Travancore deposits (Morgan Crucible Company), formerly most important: up to 13,000 tons—from 1898 to 1912, total 35,000 tons. No Travancore output since. Small output (1,318), 1916, mainly Rajputana and from 16 tons up to 252 tons in various years up to 1921, mainly from Orissa. Cost of transport militates against success of industry at present. Improved rail facilties may remedy this soon, but quality of most Indian graphite hitherto discovered (except from Sikkim) rather poor.

Uses: manufacture of crucibles (Ceylon graphite most extensively used), foundry facings, lubricants, stove polish, electric motor brushes, boiler scale preventatives, etc. Price has varied in past years up to £100 per ton, but as little as £4 per ton is common for amorphous (*i.e.* non-crystalline varietes.

Much graphite imported as (*a*) graphite and (*b*) crucibles. Over £15,000 of (*a*) and £17,000 of (*b*) annually recently, the

former partly from Ceylon and partly U.K., the latter from U.K.

Gypsum.—Found in Bikaner, Jodhpur and Jaisalmer (Rajputana); Jhelum (Punjab); Baroda and Kashmir, and in smaller quantities throughout India. Annnal production 35,000 tons to 60,000 tons, falling to 33,000 tons (Rs. 66,000), 1933. Used as fertiliser, for manufacture of Plaster of Paris and in small quantities in cement industry. Many other uses known.

Ilmenite.—Ore of iron containing titanium oxide. Monazite sands of Travancore, formerly used for extraction thorium oxide (see MONAZITE), now treated for ilmenite present. Greatly used for manufacture of white paints. Annual production, Travancore, 640 tons (Rs. 16,500), 25,307 tons (Rs. 5,00,000), 1928; 50,052 tons (Rs. 7,00,000), 1932, but declined to 43,384 tons, 1933. Present value approx. £1 per ton.

Iron and Steel.—India second in British Empire in production of iron ore. Important deposits those of Singhbhum, Keonjhar State, Bonai State, Mayurbhanj State (B. and O.); Central Provinces and Mysore. (Singhbhum deposits among most important in the world; contain from 60 per cent to 69 per cent of iron.) Annual production steadily rose from under 500,000 tons, 1914, to nearly 2,000,000 tons (1928), falling again to 1,760,500 tons (Rs. 39,20,000), 1932, and 1,230,000 tons (Rs. 25,00,000), 1933. Over 88 per cent production is from B. and O. Small quantity ore mined in Burma used only as flux in lead smelting.

Annual production of metal, approx. 1,000,000 tons pig iron, of which from 250,000 tons to 370,000 tons exported (about 50 per cent to Japan). Annual production of steel from pig-iron, from 430,000 tons to 500,000 tons. In spite of large resources, nearly Rs. 50,00,00,000 pig iron, ingot steel and manuf. iron and steel goods imported.

In recent years industry protected by bounties on rails and fish-plates wholly manufactured in India as well as on iron and steel railway wagons. Whole question of protection of iron

and steel industry much under discussion in recent years. Certain tariffs still exist on certain classes imported steels. 232,671 tons manufactured steel articles were imported in 1933.

Methods of production of pig-iron and steel in India quite equal to those employed elsewhere in world. Apparently little or no production basic slag in spite of possibilities. (See PHOSPHATES.) Further important to note that (except for ferro-manganese) no ferro-alloys (for special alloy steels) produced in India, though tungsten, molybdenum, chromium are all available. 1,432 tons ferro-alloys imported in 1933.

Lead.—Practically only source of supply in India is Burma Corp'n's Bawdin mine in Burma, one of the greatest lead-zinc-silver mines in the world. Bawdin ores contain zinc, lead, silver and copper. Reserves calculated at over 4,000,000 tons, with over 25 per cent lead. Small quantity of lead occurs also in Southern Shan States and Yamethin dist., Burma, and at Panjori, Jaipur State.

Annual production 300,000 to 450,000 tons lead ore, 454,791 tons in 1933. Over 72,000 tons lead (over Rs. 1,00,00,000) extracted in 1933, of which 65,045 tons exported. (See also ANTIMONY.)

Limestone.—See CEMENT and BUILDING MATERIALS.

Magnesite.—Important refractory. (See REFRACTORIES and BUILDING MATERIALS.) Also used as boiler lagging material, for manufacture of sulphite paper pulp and fire-resisting paint.

Manganese.—One of the most important mineral products of India, an essential in iron and steel industry. Largely used for manufacture of ferro-manganese (necessary for conversion pig-iron into steel). Georgia, in Russia, before the Great War was world's chief producer. India has twice displaced Russia, producing from 33 per cent to 37 per cent of world's total output. Sources: Balaghat, Bhandara, Chhindwara, Nagpur (C.P.); Sandur State and other areas (Madras); Keonjhar, Singhbhum, Bonai State (B. and O.); and certain districts in Madras. Annual production fallen from 1,130,000

tons (1927) to just over 218,000 tons (£123,000), 1933, due to depression. Chief competitor Russia, owing to very low selling price. Large production of high grade manganese ore now possible from S. Afr.

As regards manganese content India's ores are the best. As regards low silica content her ores stand next to those of Brazil. High phosphorus content of ores gives India low position. Present depression in India's manganese industry provides economist with mass of problems that appear almost impossible to solve. Depression mainly due both increased production by and competition from Russia and discoveries of new deposits in other countries, with consequent fall in exports.

Mercury.—See QUICKSILVER.

Mica.—India long noted for excellence of mica. Produces from 75 per cent to 85 per cent of the world's production. Important sources: Gaya and Hazaribagh dists. of B. and O.; Nellore; Nilgiri dists. of Madras; Ajmer-Merwara and Jaipur State (Rajputana). Annual production 30,000 cwts. up to over 86,000 cwts.; 32,713 cwts. (Rs. 14,35,401), 1932; 41,075 cwts. (Rs. 16,82,045), 1933. Industry suffers from great fluctuations and effects of extensive loss through thefts from mines. Chief importers: U.K., U.S., Germany and France. Mica largely used for insulating purposes in electrical industry and as heat insulator and resister. Some use as dry lubricant. Large quantities of artificial sheet mica (micanite) now made from small pieces, affecting trade in large sheets. World trade affected by increased production by S. Afr. in recent years. Interesting fact: recently as much as 4,000 cwts. mica imported by India, but imports now negligible. There would appear to be field for manufacture of mica and micanite articles in India.

Mineral Waters.—Mineral waters of undoubted medicinal value exist all over India, but no trade. Possible that by judicious advertising on large scale the mineral waters of certain districts, including radio-active waters of Tuwa, might have some commercial value.

Monazite.—Mixed phosphates of cerium, lanthanum and other "rare earth" metals, as well as thorium oxide, the latter essential for manufacture of incandescent gas mantles. Important source: Travancore. Annual production formerly as high as 2,000 tons (£60,000), practically nil in 1925. Declining trade mainly due to increased use of electricity. 90 tons (£890), 1931; 654 tons (£6,150), 1932. Recent production partly due to demand for ilmenite (q.v.) which also occurs along with monazite.

Nickel.—No very important ores of nickel yet found in India. Occurrences noted in Khatri and other places in Rajputana; Kolar goldfield; South Travancore and in the copper ores of Singhbhum. Also occurs in Burma Corpn. mines and there is steadily rising production of nickel speiss, *e.g.*, 1,000 tons in 1928 to 3,150 tons in 1930; 3,350 tons (Rs. 10,28,500), 1933. Speiss contains 25 per cent nickel, and copper, with small quantities cobalt (3–4 per cent) and silver. Considerable quantities nickel imported, especially for manufacture of 2-anna and 4-anna pieces. Annual imports over 2,000 tons nickel for manufacture of coinage. Burma speiss not treated in India. Nickel occurring in copper ores of Singhbhum not at present recovered but possibly production of electrolytic copper may render the nickel available.

Oil.—See PETROLEUM.

Paints.—(Not artists' colours.) Various ores of iron, particularly the ochres, used from time immemorial as paints. Large quantities of ochre and similar highly coloured earths suitable for manufacture of paints in India, *e.g.*, Jubbulpore; Panna State; Singhbhum and Puri (B. and O.); Hanamkonda (Hyderabad State); Myingyan (Burma). In the working of manganese ores quantities of ochres could be made available. Black slate has been used. Recent production of ochre: 1,000 tons up to over 6,000 tons; 6,237 tons (Rs. 33,110), 1932; 11,630 tons (Rs. 60,895), 1933. C.P. and C.I. are main producers. (See also ARSENIC (orpiment and realgar), BARYTES, COAL, ILMENITE.)

Petroleum.—India produces less than 1 per cent of world's petroleum, standing 11th or 12th in order of importance. Annual production just under 300,000,000 gallons (Rs. 8,46,00,000, or over £6,250,000), but insufficient for India's requirements. From 170,000,000 to 230,000,000 gallons (Rs. 8,40,00,000 to Rs. 10,44,00,000) imported. Occurrences: Burma, Assam, Punjab and Baluchistan. Burma heads list, with annual production of over 5/6 of total, Assam next and Punjab last. India's petroleum industry highly organised and resources very carefully and efficiently exploited. Owing to almost certain future exhaustion world's supplies petroleum other methods of obtaining petroleum, or substitutes, will be necessary. Known deposits may be further exploited by mining methods, and shale oil further considered. There are also unlimited vegetable and animal sources of oils and alcohols, though the latter not likely for many years to assume importance.

In 1933:—

68,818,733 gals. petrol	produced;	2,379,708 gals.	imported
139,354,915 gals. kerosene	,,	57,778,363 gals.	,,
17,699,739 gals. fuel oil	,,	104,968,758 gals.	,,
9,623,817 gals. other oils	,,	19,833,481 gals.	,,

The following import duties levied on petroleum products:—

Mineral oil for lamps and kerosene: Rs. 3/9 per gal. (there is an excise duty on kerosene of British Indian manufacture of Rs. 2/9/9 per gal.). Heavy mineral oil: Rs. 15/10 per ton up to 12½ per cent *ad valorem*. Lubricating oils: Rs. 2/6 per gal. (6 pies if from U.K.). Other mineral oils: 25 per cent *ad valorem*.

Phosphates.—Apatite (calcium phosphate) is valuable source of phosphorus for fertilising (bone ash is same chemical substance). Occurs Singhbhum, Hazaribagh and Giridih (B. and O.); Raniganj (Bengal); Trichinopoly, Nellore and Vizagapatam; Narukot State (Bombay); Jhelum (Punjab); Mussoorie (U.P.); etc. etc. Some of these, especially Singhbhum, have been worked but no record of

important trade. Note, however, large exports of bone and bone-meal, *viz.*, up to 75 per cent of total manures exports of which up to 120,000 tons recorded. Basic slag is additional source of phosphorus but not produced in India. Possibly addition of Indian apatite to blast furnace charge would give valuable supply of phosphate.

Potash.—See SALTPETRE.

Potash Minerals other than Saltpetre.—No recorded source in India. 109,716 cwts. imported in 1933.

Quicksilver (Mercury).—No recorded sources. 239,090 lbs. imported in 1933.

Rare Minerals.—Expression includes the following or their compounds: beryllium, cerium and other "rare earth" metals, columbium, gadolinium, iridium, molybdenum, niobium, osmium, platinum, radium, tantalum, titanium, uranium, yttrium, etc. Occurrences of minerals containing the above reported throughout India. Some by no means rare but their uses unfamiliar or still in experimental stage. Only beryllium, molybdenum, "rare earth" metals, and tantalum noted here.

Beryllium. Indian beryl is very high grade (see also PRECIOUS STONES) Jaipur State, Ajmer-Merwara (Rajputana); Koderma dist. (B. and O.); Nellore and Krishangarh. Uses for beryllium metal have been found in metallurgy. No production statistics.

Molybdenum. Sulphide of molybdenum, a valuable metal used in manufacture of important alloy steels. Occurrences: Wagon region (Tavoy); Chota Nagpur (B. and O.); Cherrapunji (Assam); Kunaveram, and Palni, Madura (Madras); Kishangarh (Rajputana). Only output that from Tavoy: 7½ cwts. (Rs. 1,400), 1923, none since. See also reference to ferro-alloys under IRON AND STEEL.

"Rare earth" metals. Occur in many minerals found in India, *e.g.*, at Sankara mica mine, Nellore; Yedur, Bangalore; and Tavoy, and specially in the mineral monazite at Travancore. (See reference under MONAZITE.) "Rare earth" metals

used for manufacture special alloys used as "flints" in automatic lighters. No Indian production statistics.

Tantalum. Tantalum and columbium occur, associated with iron and manganese, and rarer metals such as uranium and the preceding. Occurrences: Gaya, Koderma and Monghyr dists. (B. and O.); Madura, Nellore, Salem and Trichinopoly (Madras); various districts. Mysore and near Machil (Kashmir). Tantalum formerly used for manufacture of electric lamp filaments (now replaced by Tungsten, q.v.). Now mainly used in construction of radio and X-ray valves and neon lamps. No output reported.

Refractory Materials.—Large variety mineral substances used for furnace linings, fire-bricks, etc. Commonest is *fireclay.* (See CLAY.) High grade *siliceous rock* used for manufacture of silicia bricks and other specially resistant articles. *Kyanite* and *sillimanite* increasingly used in recent years, especially in ceramic industries. Occur throughout B. and O. Smaller quantities in Ajmer,-Merwara and Mysore. 14,000 tons (Rs., 35,000), 1932; up to 19,300 tons (Rs. 1,07,000), 1933. *Zirconium oxide* or zirconia (obtained from zircon, another important refractory). Occurs along with *ilmenite* (q.v.) in the *monazite* sands (q.v.) Travancore. Production approx. 500 tons, up to 1,465 tons (£8,129), 1927; 490 tons (£3,805), 1932; 603 tons (£3,018), 1933. *Magnesite* and associated mineral *dolomite* (double carbonate of lime and magnesia) important material for manufacture of blast furnace, linings (especially for treatment of phosphatic ores). Former extensively quarried in India, both for Indian use and for export, especially to U.S. Sources: Chalk Hills in Southern India. Very high grade obtained. Annual production from approx. 10,000 tons (1926) to 15,200 tons (Rs. 29,000), 1933. (See also ASBESTOS, BAUXITE, CHROMITE, CLAYS, GRAPHITE, STEATITE.)

Ruby, Sapphire and Spinel.—These occur together in the Mogok Stone Tract of Upper Burma. Statistics of one important company available but no record of individual workers' output. Nearly 150,000 carats (Rs. 4,67,000), 1926.

Output fallen and company ceased operations, 1931. Industry formerly chief mineral source of revenue in Burma. Kashmir another important area: 1,434,285 carats sapphire and corundum (Rs. 92,000), 1933.

Salt.—Salt industry, India's fourth most important mineral industry. Production always well over 1,000,000 tons. Occurrences: Desert region, Rajputana; Salt Range, Punjab; Kohat (N.W.F.); Madras; Bombay and Aden. Salt manufactured from sea water, *e.g.*, Bombay, Madras, Aden and Burma; from sub-soil and lake brine, *e.g.*, Rajputana and Burma; and from rock salt, by quarrying, *e.g.*, Salt Range, Punjab. Bombay is largest producer. Climatic conditions do not give promise production in Bengal. Annual consumption, 13½ lbs. per head of population, incl. salt used in agriculture and industry. Annual production excluding Aden salt: 1,712,400 tons (Rs. 1,14,25,000), 1923. Imports fell from 553,000 (Rs. 82,32,500), 1932, to 400,000 tons (Rs. 51,18,000), 1933. About 2/3 of production recovered from sea-water; rock salt accounts for about 1/8. Important source of revenue to Central Govt. Excise duty on salt Rs. 1/4 (1923) per maund, Rs. 2/8 (1924), reduced again to Rs. 1/4, but raised later: Rs. 1/9 per ton (plus temporary additional duty of as. 2½), equiv. to Rs. 42/8 (plus Rs. 4/4) per ton, 1935. No duty on salt imported for manufacturing purposes and for fish curing.

Saltpetre.—Crude saltpetre manufactured throughout India by primitive methods, decomposition of cow dung and subsequent treatment of soil with wood ashes. Bihar section of Gangetic plain specially noted. Punjab and U.P. also important. Statistics not now recorded but nearly 190,000 cwts. (Rs. 15,60,000) exported, 1933. Some used in tea-gardens in India and for manufacture of gun-powder, especially in coalfields and other mining areas. Small quantity imported by sea and more from Nepal, *e.g.*, nearly 4,000 cwts. per annum in recent years.

Sapphire.—See RUBY.

Soda.—Soda, like sulphuric acid, an essential in many important industries (*e.g.*, soap-making, glass-making, etc. etc.) and India deficient in deposits. Alkaline soil-surface deposits at Champaran, Muzzafarpur and Saran State (B. and O.); Benares, Azamgarh, Janupur, Ghazipur, etc. (U.P.); Lower Lake, Berar; Khairpur State, Sind; Sambhar Lake (Rajputana). Approx. 750 tons soda compounds from Khairpur State in recent years. Rs. 1,50,000 to Rs. 1,75,000 compounds exported annually from Karachi. From 50,000 tons to 75,000 tons soda compounds imported annually.

Establishment of a soda industry in India is a pressing necessity for development of many other industries on an economic basis.

Steatite.—Mineral of varied uses, *e.g.*, potstone (for making dishes, pots, etc.) soapstone (for carvings), and (the hardest form) for gas burners. Also used in manufacture of lead pencils, and one variety is talc. Manufacture of domestic articles is largely a village industry, and no records are available. Bricks made of steatite also used for furnace linings. Occurrences: Idar State (Bombay); Jaipur State (Rajputana); marble rocks, Jubbulpur, Gowari and Lalpur, south side Narbada river; Pakokku hill tracts, Burma; Maddavan and Betamcherla, and Salem (Madras). Production variable—from 3,000 tons (Rs. 71,000) to 17,000 tons (Rs. 1,83,000), 1933.

Sulphur, Sulphuric Acid and Sulphates.—Enormous quantity sulphur essential in industry but India possesses practically no supplies of natural sulphur. Sulphur formerly mined at Barren Island, Bay of Bengal, and Kalat State, Eastern Baluchistan. Supplies of sulphur would be of great value to India. Other possible sources of sulphur are metallic sulphides, *e.g.*, iron pyrites, copper pyrites, zinc concentrates, etc., and sulphates such as gypsum, barytes, etc. Important industry is manufacture of sulphuric acid which in turn is essential in other heavy chemical industries. Many plants for manufacture of sulphuric acid started in recent years in India but sulphur practically all imported. Annual import 10,000 tons to 25,000

tons; 20,200 1933. This does not include ammonium sulphate, of which 1,640 tons imported, 1933. Sulphur imported mainly from Sicily, Japan and Germany. During treatment of copper and zinc ores much sulphur dioxide, equivalant to upwards of 3,000 tons of sulphur at present which could be converted into sulphuric acid, escapes into air. (See also ALUM, ALUMINOUS SULPHATES, ETC., and ZINC.) Sulphur is not liable to import duty.

Tar.—See COAL.

Tin.—Practically the only source of tin is cassiterite (tinstone) deposits of Burma. Ore is mined and treated to obtain concentrates for export (not for smelting). Formerly some smelting to obtain tin took place. Annual production tin ore risen rapidly since Great War: 4,500 tons (Rs. 45,10,000), 1932; 5,000 tons (Rs. 71,00,000), 1933. Large quantities block tin imported annually; from 2,000 tons to 3,000 tons; 2,500 tons (Rs. 47,50,000), 1932; 2,080 tons (Rs. 53,00,000), 1933. Practically no workable deposits of tin ore in India proper.

Tungsten.—Tungsten ore, wolfram, occurs along with tin ore, q.v. Important district, Tavoy; Southern Shan States also. Tinstone and wolfram deposits carefully treated to obtain tin concentrates and wolfram concentrates separately. Annual production 2,023 tons (Rs. 7,04,000), 1932; 2,147 tons (Rs. 10,84,639), 1933. Tungsten metal specially valuable for manufacture of high-speed tool steel. Tungsten compounds also used in chemical industries, dyeing, fireproofing, and in manufacture of electric lamp filaments.

Zinc.—Only deposits those of Burma Corp'n. at Bawdwin Mine. Zinc concentrates produced at Namtu. Annual production of concentrates has risen rapidly from 20,000 tons to about 60,000 tons; 61,432 tons (Rs. 30,83,000), 1933. Zinc metal not smelted in India, though much zinc required for manufacture of brass. (See COPPER.) Copper and zinc smelting in India could provide sulphur dioxide gas for manufacture of sulphuric acid.

CHAPTER XXI

INDUSTRIAL FINANCE IN INDIA

By Dr. Nabagopal Das, Ph.D., I.C.S.

Introductory

In recent years no question in India has perhaps raised so much controversy as the problem of financing her many growing industries. Businessmen and politicians of almost all shades of opinion have been persistently demanding the establishment of special banking institutions on the German or Japanese model in order to finance industry and have also been shouting that the present system of industrial control by certain vested groups should be ended as soon as possible. In these controversies sound and rational economic thinking has often been blurred by ulterior political considerations and not infrequently the basic difficulties or shortcomings of industrial organisation in India have been overlooked or lightly brushed aside.

The problem of financing industrial operations in India is of very recent origin. There was no such "problem" in the days before the coming of the economic transition, and for a considerable time after the industrial changes arrived, the subject did not assume the vastness or complexity of a real problem. Even a very cursory analysis of the industrial history of India from the days of the early economic transition to the beginning of the present century would bear this out.

An Historical Survey.

Before the coming of the economic transition there were no organised industries of the type of modern capitalistic enterprises and all "industries" were either cottage industries or unorganised industries. Almost

all industrial activities of those days were confined to simple purchase and sale, and the various crafts that flourished in the villages served mainly local needs. The artisans were mostly village servants, doing all the miscellaneous duties connected with their occupations in the villages and the division of labour was extremely limited. There were no problems of finance in the urban industries either. Most of the urban industries were controlled by merchant guilds and a merchant guild would consist of all the merchants, bankers and large dealers of a city. These guilds had central funds of their own, derived from fees and imposts, but these funds were scarcely, if ever, employed in industrial finance proper; they were more often meant for "social and religious activities". The guilds, however, controlled the output of merchants' wares, determined rates of sale and amounts of marketable material and were undoubtedly "indispensable to the advancement of the middle classes in their struggle for recognition at the hands both of despotic kings and of an organised priesthood that was bent on suppressing the elevation of the third caste." They solidified the communal character of trade and industrial enterprise, and, although they did little for the actual financing of industry, their services towards the maintenance and development of organised production and fairly stable markets were by no means insignificant. As capital played a very small part in the manufacture or actual turnover of goods, there was no problem regarding the supply of capital to industry. Much more important than capital were skill and connexion, the ability to produce good wares and the steady demand of a small group of customers.

The economic transition came in India very slowly—long after the establishment of British rule in the Ganges delta. First of all, the competition of machine-made goods imported into India from Europe dealt a severe blow to the native crafts and industries: the indigenous industrial system was dislocated and the wealthy financiers or bankers of old days were gradually reduced to the status of ordinary money-lenders. The currency and exchange situation was soon in a flux and organised trade and industry became wellnigh

impossible for a time. The establishment of the Agency Houses in Calcutta, consisting mostly of partners from amongst the civil, military and medical officers of the East India Company, gradually brought some order to the chaotic state of mercantile enterprise, but even this was short-lived. The Agency Houses and the early European joint-stock banks engaged themselves in an ugly competition for getting the utmost out of their capital and this led to speculative dealings and improvident advances, with the result that by 1840–41 almost all of them collapsed. Their failure, however, was an important pointer to the fundamental lack of equilibrium in the economic position of the country. While there were vast sums of available funds in the hands of the Agency Houses and banks, there were no adequate opportunities for investment at all. Economic life had been disorganised by the impact of machine-made products from the West as well as by the weakening of the indigenous economy; and while old industries were dying, few new ones (except perhaps the indigo industry) were taking their place. On the other hand, both the Agency Houses and the banks had been confronted with the problem of how to employ their capital and deposit resources. In the anxiety to make profits, they gave up the rôle of pure bankers and became merchants and sometimes even indigo-planters and shipowners. This vicious combination coupled with the fact that there were no avenues for safe but profitable investment of all the available surplus brought ruin upon these early financing houses.[1]

From about the middle of the nineteenth century, however, the industrial development of India in its essentially modern sense may be said to have made a start. An Act was passed in 1857 conferring the privilege of limited liability on joint-stock associations in general and in 1866 a further consolidated Indian Companies' Act was passed. All these pointed to the fact that a new industrial life had commenced in India and the whole of the second half of the nineteenth century was characterised by the investment of British

[1] For a detailed survey, *vide* my *Banking and Industrial Finance in India* (Calcutta, 1936), Chapters II-V.

capital and the employment of British private enterprise in the mines, factories and manufacturing concerns of India. During all these years, however, Indian capital played a very unimportant part in the industrial development of the country, and, except for the solitary instance of the cotton textile industry of the Bombay Presidency, almost all the concerns were financed with British money and managed by British firms.

The problem of industrial finance did not present itself even towards the end of the nineteenth century. Under the peculiar circumstances of the economic development of India during this period, there had arisen an ingenious system of finance and management called the "Managing Agency system." These were old and well-established firms (mostly British) at the important Indian ports hitherto concerned mostly with the external (and sometimes also internal) trade of the country. Now, the new joint-stock companies began to look to the public for money for the promotion of specific enterprises, but at the same time they preferred the risk to fall on others; on the other hand, British promoters (especially of small and new ventures) were only too glad to have the backing of the name of these big, well-established firms and were only too eager to link the larger organisation with their own. Moreover, the fact that most of the promoters of new ventures remained in India only for a short period and had a very imperfect knowledge of the peculiarities of Indian business and industrial enterprise made it almost imperative that the actual management of the new projects was to be handed over to old firms of established reputation and experience. The actual promoters of a company would raise the necessary initial capital, while the Managing Agents would, by their Articles of Association, undertake to manage the venture on behalf of the company in return for an annual sum for office expenses and a commission on output, sale or net profits. These firms facilitated continuity of policy, conduced to efficient and economic management, and even helped a concern with their own funds in times of temporary stringency or difficulty. The

Indian Agency firms, organised more or less after the European houses, went a step further. While actual figures or details as to the extent to which an Indian Managing Agency firm of Bombay or Ahmedabad "financed" a particular mill are not available, it seems that most of the working capital came from the Managing Agents, although a considerable proportion of the block capital was derived either from private deposits or from the public purchase of shares. There was, therefore, on the whole, no difficulty in financing the industries that had come into being.[1]

As the years rolled on, however, to the beginning of the twentieth century, certain new factors altered the whole situation. In or about 1905 the full effects of railway development in India began to be felt and the economic policy of the Government of India also began to undergo a new orientation. It was in this year that the *swadeshi* movement came and a direct consequence of this was the flow of Indian enterprise in the organisation, management and finance of India's own industries. As difficulties began to be encountered, criticism was levelled at the banking and financial policy of the Government of India and people began to ask why capital was so shy and industrial development so sluggish. It was then, and then only, that the problem of financing industry assumed its truly modern proportions. The year 1905 opened the floodgates of Indian enterprise and it was pertinently asked whether it was the paucity of suitable banking institutions that hampered industrial finance or whether it was the imperfect economic development of India that prevented a harmonious growth of banking institutions. A series of official enquiries followed from 1913 onwards and in each of these enquiries the problem of financing India's industries loomed large in the foreground. Indian enterpreneurs began to demand that either the existing banks should come forward with a bolder and more vigorous policy or that Government should set up special institutions for the provision of finance to the industries of the country.

[1] For a detailed survey, *vide* my *Banking and Industrial Finance in India* (Calcutta, 1936), Chapter VII.

THE PROBLEM OF INDUSTRIAL FINANCE

It will be opportune now to enquire what the financial requirements of the more important industries in India are and how they are met. "Broadly speaking, industries require capital for two purposes—(1) capital for block, that is, to finance fixed assets, and (2) working capital, that is, to finance floating assets. Block capital is required by newly started industries for fixed assets, such as land, buildings, machinery and other appliances of a durable and permanent character. It is also required in the case of established industries for purposes of extensions and replacements. Working capital is required for the purchase and working up of raw materials into finished products, for stores, for expenses incidental to the marketing of products, for financing outstanding operations in respect of goods supplied, and for providing the necessary funds for meeting day-to-day requirements. The capital that is invested in this latter way is of the nature partly of permanent or long-term capital and partly of short-term finance."

So far most of the major industries in India have obtained their capital for financing fixed assets either by public or private subscription of shares or debentures of the undertaking, or by direct deposits, or by the system of providing money on private account by an individual or a partnership. The part played by these diverse methods has of course varied from industry to industry and the recent tendency has been towards securing the block capital by public or private subscription of shares or debentures.[1] In the cotton textile industry, for instance, apart from the few older establishments which still retain their private proprietary character, the fixed capital has been found mostly from paid-up share capital, though in some cases this has been supplemented by debentures. Except a very few mills which have a portion of their capital in preference shares,

[1] Detailed figures are given in my *Industrial Enterprise in India* (London, 1938), Chapter I.

the share capital consists entirely of ordinary shares of face values varying from Rs. 25 to Rs. 1,000 per share. There has been a commendable tendency in recent years to split up shares of larger face value into shares of smaller denominations with a view to bringing them within the easy reach of small investors. In some cases extension of the fixed plant and machinery has been wisely provided out of issue of preference shares at a time when the companies concerned had established a sound reputation by their unbroken record of dividend payments. Sometimes debentures have been issued for limited periods on the security of the fixed assets consisting of land, buildings, plant and machinery for the same purpose of extension or for the introduction of new devices.

In the iron and steel industry, too, share capital (including preference shares, and ordinary and deferred shares) has provided nearly all the money needed for financing fixed assets, and the experience of the hydro-electric industry has also been the same. On the other hand, cases are not rare where even fixed assets are financed by direct deposits from the public: this obtains particularly in the cotton mill industry of Ahmedabad.

Lastly comes the method of providing money on private account by an individual or a firm or a partnership: this was much in vogue in India when the joint-stock principle was not properly appreciated, and many of the plantation industries like tea, coffee and sugar, and some of the mining enterprises have, in the past, been launched in this manner. Even nowadays many small ventures are started with assets financed by money secured on private account by an individual or a firm or a partnership. Many of the rice mills, oil mills, hosieries, soap factories, etc., are run on an individual proprietary basis, the owner bringing his own capital for meeting such initial outlay as is necessary for acquiring land, setting up the factory, purchasing machinery and raw materials and providing other equipments.

As regards the working capital, this is obtained either from private deposits, or from money on private account provided by the entrepreneurs and their friends, or from

loans given by commercial banks and indigenous bankers. In the cotton textile industry the working capital is obtained from two sources—(1) deposits; (2) bank loans and cash credits. "With very few exceptions cotton mill companies generally depend for their working capital to a considerable extent on deposits received from the public. These deposits are in most cases from six to twelve months and the rates vary with the credit of the individual mills and of their Managing Agents. . . . Public confidence, till very recently, was so well established that good mills were able to obtain deposits not only at the same rates as quoted by banks but in some cases even ½ per cent cheaper than banks." Besides these deposits from the public most of the mills in Bombay and up-country centres have certain arrangements with their banks by which they obtain loans on the security of stocks of cotton and cloth, either manufactured or in process of manufacture. "In some cases loans are raised on gilt-edged securities deposited with banks; in others, only on the promissory notes of the company with a copy of the resolution passed by the Board of Directors." In most of these cases, however, banks insist on the additional guarantee of the Managing Agents over and above the stocks hypothecated by them.

In the iron and steel industry where the requirements of working capital are very large the problem of finding finance has always been very acute. The Tata Iron and Steel Company had once to seek Government assistance for working its plant and this took the form of "a fixed loan of Rs. 50 lakhs by the Secretary of State for India with whom the Company deposited an equivalent amount of its unissued debentures." In the sugar industry, on the other hand, most of the working capital has generally been found from banks and the various firms of Managing Agents which control the companies. Far more fortunate has been the position of the jute industry: having invariably started with large capital, jute mills in India have never had any difficulty in getting temporary accommodation from banks. The reputation and standing of their Managing Agents have also been valuable assets in securing the requisite finance.

On the other hand, many of the newer enterprises and smaller concerns have had to contend against heavy odds in securing the necessary working capital for themselves. It is not an exaggeration at all to say that most of the industries that have not had the advantage of an early and favourable start, have to experience great difficulties in securing finance. The Indian Steel Wire Products Ltd., for instance, could not increase its output during the cold weather of 1923–24 mainly due to a shortage of working capital and the difficulty had eventually to be removed by the Government of Bihar and Orissa sanctioning in August, 1924, a special loan under the Bihar and Orissa State Aid to Industries Act. Even the sound concern of the Tata Iron and Steel Company had to contend with very serious financial difficulties for a number of years after the War. And in the paper and paper pulp industry the financial predicament of the chief concerns could be solved only by a Government guarantee of a public issue of debentures. In the plywood and tea-chest industry, too, money has been obtained with considerable difficulty: an ordinary manufacturer has hardly been able to borrow money over an extended period at a rate within 1 per cent of the official Bank rate.

As a matter of fact, loans have often to be dearly paid for, whether they are obtained from indigenous bankers or joint-stock banks, or as deposits from the public. In the tea-gardens belonging to individual proprietors, for instance, loans are obtained from *marwaris* and other indigenous bankers only at rates varying from 12 per cent to 20 per cent (according to the credit position of the borrower) and even then the personal security of the proprietor has sometimes to be coupled with a mortgage of the garden property. Loans obtained from loan offices are secured at somewhat lower charges, but there, too, the personal guarantee of some directors and the mortgage of the gardens as collateral security are considered essential. Sometimes Managing Agents provide for the finance as well as sale of crops of some of these tea-gardens, but that only means that the enterprises so financed lose all their independence in the matter of production, sale and marketing. Particularly

unfortunate is the lot of those concerns which, being newly started, cannot approach either the selling brokers or the loan offices with their limited assets and hence have to borrow at very high rates of interest from indigenous bankers who not only cover their loans by the double security of mortgage and personal guarantee but also insist occasionally on a fairly large commission on future sales.[1]

Nor should it be imagined that industries that are owned and managed by joint-stock companies fare better by virtue of their corporate organisation. "The realisations from their share flotations do not enable them to meet all capital requirements and their dependence on outside finance is no less marked than in the case of similar establishments owned by individual proprietors. Loans are available to the companies only when some directors agree to pledge their personal guarantee as cover. And when such loans are obtained from indigenous bankers they charge the same rate and stipulate the same conditions as are demanded from, and imposed on, the individual proprietor."

MANAGING AGENTS AND INDUSTRIAL FINANCE

We have seen that Managing Agency firms in India play an important part in the matter of industrial finance. Cotton mills in India are dependent largely on the standing of the Managing Agents for the funds they require much more than in other countries more advanced in banking matters, and even in such industries as jute, iron and steel, coal and sugar the backing of the name of a reputed firm of Managing Agents generally facilitates access to credit. Not infrequently Managing Agents themselves have to advance funds in times of difficulty or distress.

The services rendered by Managing Agents in the sphere of finance have not, however, been an unmixed blessing. Apart from the fact that such advances as are made are never disinterested, it is notorious that such facilities as the ordinary joint-stock banks are generally prepared to

[1] Detailed figures are given in my *Industrial Enterprise in India* (London, 1938), Chapter I, pp. 13–15.

offer to industries are not utilised by them, because many Managing Agents argue that this involves visible control by the banks, lowers their standing in the eyes of their creditors and the investing public, and increases the difficulty of obtaining fixed deposits! Moreover, although it is true that in times of crises Managing Agents have incurred extensive losses as a direct result of financing the mills under their control, there have been cases in which these Agents have surreptitiously turned their loans to mills into debentures, with the result that the concerns have virtually passed into their hands. The system of Managing Agency finance may work well when everything goes on smoothly and when industries are prosperous, but in times of depression when Managing Agents are compelled to find more money to support them, it often happens that they are unable to cope with the situation.

The question of finance by Managing Agents brings us to another system—the system of direct deposits that prevails in the cotton textile industry of Bombay and Ahmedabad. The system arose owing to the imperfect banking development of the country: on the one hand, people naturally had more trust in, and preferred to confide their savings to, those men in their communities whom they knew and with whom they could deal without the formalities necessary in dealing with banks; on the other, mill-owners were ready to accept deposits from the public because most of their concerns were undercapitalised and they were under a moral obligation to find the requisite working capital for them. So arose an arrangement whereby the cotton mills of Bombay and Ahmedabad got most of their working capital from the public on short-term deposits, usually for six months or a year.

The recent depression in the cotton textile industry has exposed the inherent weakness of the system of finance by direct deposits. In times of stringency mills whose financial position is not strong, find great difficulty in obtaining deposits, although it is these mills which need most help; again, the tendency of depositors to withdraw their advances on the slightest rumours puts mills in a most

unenviable position. They cannot raise loans elsewhere in a period of depression and thus they are faced with the grim alternative of closing down entirely or spoiling their credit for all time to come by refusing to pay back to the depositors.

SOME GRIEVANCES ANALYSED

Let us now analyse what views industrialists hold about the financial facilities they enjoy. The most marked divergence of views appeared in the replies to the question whether existing facilities were adequate when the Indian Central Banking Enquiry Committee was holding its sitting. While representatives of European Chambers of Commerce took the view that financial facilities were more or less commensurate with the economic development of the country, most of the Indian entrepreneurs complained that, except from Managing Agents and direct depositors, financial accommodation has always been difficult to obtain in India. It was regretted that banks in India did not provide finance for block capital for industries and that conservatism and timidity prevented them from embarking on the underwriting of industrial capital or at least of lending money on the security of industrial shares to any great extent. Another complaint was that banks usually insisted on a full backing of tangible and easily realisable security for loans and seemed to take no account of the personal credit and integrity of borrowers. Moreover, it was pointed out that trade demands generally act to the disadvantage of industry, having taken the lion's share out of a limited available surplus, and sharp fluctuations in interest rates owing to seasonal variations in trade also handicap industrial development. The complaint was not merely that industry felt that it was not receiving adequate finance; it was also that available finance could be obtained only at a very high price.

A close analysis would, however, show that many of the alleged defects cannot be laid at the door of existing financial agencies. The argument that banks should provide finance for block capital is against all canons of financial

propriety; initial block capital should always be put up by public or private subscription, and even in Germany, which is held to be the model India should follow, none of the banks provide finance for block capital. Their share and syndicate operations are in the nature of guarantees only: they never supply the initial block capital themselves.

As regards the complaint that joint-stock banks in India insist on a full backing of tangible and easily realisable security, it is difficult to see how things can be improved when the series of crises that have occurred in the past owing to bad and speculative advances are taken into account. Perhaps their policy is a bit too cautious and conservative, but "the restrictions imposed by the necessity of conforming to conservative methods of banking have promoted a healthy growth which would have been absent from any form of subsidised assistance unless guided by a staff of experts as in the case of the German credit banks." Moreover, it is a fact that the expert help and guidance which are available to German credit banks are not obtainable in India to-day, and this again is due to the more fundamental reason that scientific and managerial experience in the various lines of industrial activity is still rare in this country.

The reason why joint-stock banks in India do not grant any long-term credit to industries is obvious It is almost a truism that good banking presupposes a series of self-balancing transactions, and hence ordinary joint-stock banks whose assets consist largely of customers' deposits liable to be withdrawn at short notice, cannot, without incurring serious risks, lock them up in long-term advances or loans. It should not be overlooked that in countries like Germany where joint-stock banks make some sort of long-term advances to industry, these particular transactions are conditioned and limited by the nature and extent of that proportion of their capital and deposits which are not likely to be recalled for certain definite periods of time. Moreover, even in Germany the larger financial transactions of these banks (*e.g.*, the promotion of companies, the taking over of new capital issues and of obligations of existing companies, the guaranteeing of public loans, etc.)

are definitely subordinate to their ordinary commercial operations. It is no wonder, therefore, that Indian banks with a poorer equipment and an infinitely more uncertain investment market should hesitate to embark on long-term industrial commitments.[1]

THE NEED FOR A BOLDER POLICY BY BANKS

This defence of existing practices does not mean that all is well, nor does it establish the thesis that no further improvements can be made in the present state of our industrial development. The absence of a real Central Bank was the most formidable drawback so long and the system of dual responsibility of the Government and the Imperial Bank of India which existed until recently was far from satisfactory. The newly established Reserve Bank of India is expected, by a mobilisation of the banking and currency resources, to mitigate the evils of a fluctuating and high price for the use of credit available for trade, industry and agriculture. And the existing joint-stock banks will, it is hoped, now be able to meet the financial demands of industry better by virtue of the increased facilities they would be getting from the Reserve Bank through the re-discounting of bills.

A bolder policy should forthwith be adopted by the Imperial Bank of India and some of the more important Indian joint-stock banks. Now that the Reserve Bank has been established, the Imperial Bank of India has been relieved of a number of important statutory responsibilities. It should forthwith start making a survey of the financial needs of various industries and also commence doing the German type of mixed business. More than any other bank in India, it has got experience and an established policy and tradition of sound banking: it is most admirably fitted, therefore, to take upon its shoulders the burden of doing some real industrial banking. It need not act alone, but it must take the lead and set an example to other banks which are strong enough to follow in its footsteps.

[1] Detailed figures are given in my *Industrial Enterprise in India* (London, 1938), Chapter II for an exhaustive analysis.

It will also be necessary for the Indian entrepreneur to change his outlook. The habit of the average Indian dealer or entrepreneur to resort by preference to the *shroff* who sits in a little bazaar shop rather than "expose himself to the enquiries, the regularised procedure and (as he believes) the greater risks of a joint-stock bank with a grilled counter and a uniformed peon in the doorway" must be abandoned. How can the question of lending on the personal security of the borrower be even put forward to a bank when he (the borrower) is unwilling to tell the details of his business to his creditor? Even in the West the granting of clean credits is confined to big firms of undisputed standing. As things stand, a long time must elapse before the undoubtedly weaker banks of India are in a position to grant clean credits to the average entrepreneur.

Another method whereby the problem of industrial finance in India may be partially solved is by evolving a type of negotiable instrument which would be acceptable to all banks, the value of which would not depend exclusively on the standing and respectability of the borrower, and which would be something more than mere paper. Such an instrument is obviously the commercial bill, but in India the method of obtaining money by discounting commercial bills has not been properly explored yet. Until the Reserve Bank of India was established, a very real difficulty stood in the way of developing a good bill market in this country. Banks were reluctant to discount bills because they could re-discount them only at the Imperial Bank of India, and they did not like that the said bank, their rival so far as commercial business was concerned, should know their bill portfolios. With the establishment of the Reserve Bank of India and the facility that *all* banks now get to have their bills re-discounted at the Reserve Bank, this difficulty should disappear and it should be possible for firms to obtain credit by the convenient method of getting their bills discounted.

The problem, however, is to make the bill represent something substantial—real value in non-perishable, readily saleable goods. This can be achieved by basing the credit

system on valuable and liquid assets such as bonds, shares and movable goods. In certain countries (e.g. Java) where no true money market and no inland bills exist, loans and advances are made against warehouse warrants or warehouse receipts representing such assets. India, too, should develop the method of licensed warehousing: firms requiring temporary accommodation should store their raw products or manufactured articles in these warehouses, and the receipts issued against them should be used as collateral for loans which commercial banks are ordinarily able to make on the strength of covered bills. An organised and well-managed system of warehousing should enlarge the basis of credit and facilitate the grant of short term advances by banks to industry and trade.

THE CASE FOR A STATE-AIDED INDUSTRIAL BANK

In all discussions about industrial finance in India one point has always been urged by politicians and businessmen: it is that an Industrial Bank should be established by Government to finance new industries and also to help such old industries as are intrinsically sound, but have fallen on evil days for reasons beyond their control. The arguments advanced in favour of establishing such an institution are many and various. Indian capital, it is said, is shy and only an Industrial Bank could mobilise it and turn it into productive channels of investment. Such a bank, it is urged, would be of immense benefit to the country in guiding its industrial development on sound lines. "It would be able, by its experience and knowledge gathered from all parts of India and tabulated by a well-equipped intelligence department attached to the bank, to act as a guide and friend to all industrial concerns in India, young and old. It would prevent uneconomical and wasteful efforts to start industries in places where there are no possibilities and it would itself be in a position to formulate schemes for industrial development besides analysing and criticising propositions placed before it for financial assistance and support." The establishment of an Industrial Bank with

Government participation in its share or debenture capital, or Government guaranteeing interest on its debentures, is expected also to inspire confidence in the investor anxious to invest in securities of an industrial nature—a confidence that is singularly absent in India for a variety of reasons.

Now, certain general observations on the project of such an Industrial Bank or Corporation will not be out of place here. A considerable proportion of its share or debenture capital will have to be taken up by Government, or interest on its debentures will have to be guaranteed by it. Direct financial participation of this nature by the State is of doubtful utility and it is important to recognise that if Government participates in, or guarantees, the capital issues of such a bank, it will have to encroach on affairs which should properly belong to private enterprise. Nor should we forget that in India industrial organisation is still backward and the range of choice for investments limited. Those who pin their faith in an Industrial Bank or Corporation tend to forget that of the hundred and odd banks which failed during the six years from 1922–27, a large percentage was brought down by investments in industrial enterprises.

The fact is that the starting of industries is never a bank's affair: an enterprise that wants accommodation must possess a certain minimum of block capital and working capital before it can hope to get help from a bank. Moreover, it is sheer foolhardiness to overlook the fundamental economic fact that, with an efficient investment market lacking, no amount of State guarantee can make a bank of the proposed type work successfully. What is really needed is an energetic body of entrepreneurs who are prepared to risk their own money and stand on their own feet, *i.e.*, without subsidy and without protection of any sort. It should not also be overlooked that condition for the development of industrial banks is that there should first be a large and efficient organisation of ordinary deposit banking in the country. No form of banking can develop and flourish except through an organic growth, and while the natural desire of Indians to accelerate the industrial development of the country is perfectly understandable, we

cannot afford to shut our eyes to realities, nor can we ignore the strain that any bolstered-up scheme is likely to impose upon the economic machine of the country. State help is certainly useful and should be exploited with profit, but the natural movement of economic forces cannot also be lightly ignored.

CONCLUSION

The important point to remember is that the problem of industrial finance is a problem not only of the mobility of the financial resources of a country but also of their quantity and quality. We may complain loudly that industry does not always get the finance it requires at a reasonable price, but as long as the earning capacity of the people, their will to save and the incentive to save remain feeble, we cannot hope for any appreciable improvement of the present situation. Firstly, India is inherently poor, which means that there are not many in the country who have a surplus to save. Secondly, the desire to save is conspicuously absent among certain classes and, even where it exists, it is diverted to wrong and unprofitable channels. Finally, there are no institutions in India which can make a scientific study of the character and mentality of the admittedly shy potential investors and present industrial propositions before them in a really attractive form. Until the problem is tackled at these ends, all industrial ventures are likely to founder on the rock of so-called financial difficulties.

The close connection between industrial finance and industrial management should not also be overlooked. It *is* a fact that the gross mismanagement of some of our industrial concerns has been directly responsible for the general shyness of investors and has accentuated the recent financial difficulties of some enterprises. If those who are at the helm of industrial undertakings to-day would manage them more efficiently and with a greater degree of honesty, many of their financial obstacles would readily disappear.[1]

[1] Detailed figures are given in my *Industrial Enterprise in India* (London, 1938), Chapter VIII.

CHAPTER XXII

INDUSTRIAL LABOUR IN INDIA

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I

Lines of industrialisation.—The remarkable developments in the sphere of industrial production which characterised India's economic life during the last quarter of a century have been dealt with elsewhere in this series of essays. In order, however, to provide a background for our study of the problems connected with industrial labour, a short summary of the present situation as regards industrial activities may here be attempted. India is an agricultural country, but the nature of the crops sown affords a clue to the lines along which industrialisation has advanced. A tenth of the land tilled is under cotton, and the vast riverine areas of the north-east corner of the peninsula are covered during the season with waving fields of jute. This growth of cotton and jute has led the way to the creation of a great textile industry. There were, in 1936, 379 mills equipped for the manufacture of cotton yarn and cloth, with over 9·8 million spindles and 200,000 looms; the number of operatives employed daily on day-shift work only was approximately 418,000; and the capital investment in the industry, including share capital, debentures, loans and deposits, may be estimated as being in the neighbourhood of Rs. 75 crores. An equally impressive tale may be told of the jute industry; there are just over 100 jute mills in India, the majority of which is situated in Bengal. At the beginning of 1936 there were in Bengal alone about 61,000 looms and 1·2 million spindles; the

average daily number of hands employed was over 242,000; and over Rs. 23 crores have been invested in the industry as share capital and debentures alone, not to mention capital investments from other sources. Jute manufactures in value represented 14·6 per cent of the total exports of merchandise from British India in the year 1933–34, and 14·2 per cent in 1934–35. Cotton and jute textiles, however, do not by any means exhaust the list of India's industrial achievements based on agriculture; and as further illustrations of the way in which the crops grown have led to the creation of corresponding industries may be mentioned "the plantation industries"—principally tea and rubber, the production of which came to 400 million and 37 million lbs. respectively in 1934. Prominent mention should also be made of the great mining industries of the country (particularly coal-mining which gave employment to over 229,000 persons in 1934); the total mineral output of the country was valued at 24 millions sterling in 1928, and even in 1934 stood at about 18 millions sterling. India possesses, besides, flourishing iron and steel works, foundries, railway workshops (which employed over 104,000 persons in 1934), dockyards, tanneries and leather factories, petroleum refineries, and rice mills. Impressive additions to India's industrial equipment in recent years have been the sugar industry, the number of factories engaged in which rose from 45 in 1929 to 225 in 1934, and of workers from 15,076 to 65,023 during the same period, while the production in 1936–37 was nearly 21 million cwts.; and the cement industry, the production of which, in the same year, amounted to 997,000 tons (the recently formed Indian cement merger—the Associated Cement Companies—has a capital of 8 crores of rupees, and is said to have a productive capacity of 1,465,000 tons per year). In a lesser category are the paper industry, employing a capital of about Rs. 3·8 crores and producing 962,000 cwts. in 1935–36, and the match industry. Altogether, India has definitely taken rank as a manufacturing country, and the Council of the League of Nations has included her among the 8 States of "chief industrial importance" in the world.

Estimate of industrial population.—Let us now turn from these abundant indications of industrial progress to the human element involved in the processes of production. To form an estimate of the numbers engaged in the various productive processes, a reference may be made to the occupational table in the Census Report of 1931. It is enough for our purposes to cull a few figures from this statement. Out of the total population of 351 millions recorded in 1931, 125 millions are reckoned as "earners" and 29 millions as "working dependants." The total number engaged in cultivation, with its subsidiary occupations, is 103 millions, of whom 97 millions, including about 31 millions of agricultural labourers, are actual workers. There are, besides, about 1·7 million actual workers engaged in the cultivation of special crops, of which over a million is employed in tea cultivation alone. The extraction of metallic and non-metallic minerals provided employment for 404,000 persons, of whom 346,000 were actual workers; industries for the colossal figure of 17·5 millions, of whom 15·3 millions were actual workers; and transport for 2·8 millions, including 636,000 actual workers employed on the railways and 362,000 actual workers employed on transport by water. These figures are sufficient to show that India's working population is much larger than that of any other country in the world; but it is well to remember that they cover all kinds of industrial pursuits carried on both in big factories and in smaller units. The number of workers employed in "organised labour" is extraordinarily low for a population the size of India's. The total figure for persons occupied in plantations, mines, industry and transport in 1921 was over 24 millions, of whom only 2·7 millions were employed in mines, plantations or organised industrial establishments having 10 or more employees. The total figure under the three same heads for 1931 amounts to 26 millions, and if labour in similar establishments is in the same proportion, it should have been about 3 millions in 1931. The census authorities are of opinion that probably 5 millions may be taken as the figure for organised labour in India in 1931, as the figure

normally available refers only to the daily attendance in registered factories. The statistics of factories under the Factories Act in 1935 show the average daily number of operatives attending factories during the year as 1,610,932; the average daily number of persons working in and about the mines regulated by the Mines Act in 1935 was 253,970; and to these may be added the railway workers, numbering about 700,000, and the plantation workers, numbering about a million. For the purposes of this study, the total of these figures may be taken as representing the strength of organised industrial labour in the country, or at least of that section of organised labour regarding which definite information of some kind is available. Nor is this labour force so very widely scattered as one may be tempted to imagine from the vast extent of the country. About half the factory population is concentrated in the urban and suburban areas of Calcutta and Bombay, while up-country manufacturing towns like Ahmedabad, Cawnpore, Jamshedpur, Madura, Coimbatore, as also some capital cities, as Madras, Delhi, Lahore, Lucknow and Nagpur, account for a great part of the rest. The coalfields of Bihar and Bengal and the plantations of Assam and the extreme south of India are naturally the centres of the mining and plantation populations respectively.

II

Labour supply.—One would expect that India, with an agricultural population "greatly in excess of what is really required for the thorough cultivation of the land," would be able to provide an abundant supply of industrial labour. As a matter of fact, industrial labour has always been almost entirely recruited from the agricultural areas. There is a growing class of agricultural labourers who possess no land of their own, and with the increasing pressure of population on the land, a great many of them are compelled to turn to industrial avocations for gaining their livelihood. To these should be added the smallholders deprived of their strips of land through the operations of the money-lender,

the rent-collector, or the tax-gatherer. Another stream of labour supply comes from the break-up of the old village organisation which forces the village artisans and menials to better their position and prospects by seeking employment in the urban areas. In spite of these prolific sources of supply, Indian industry, until just after the War, was faced with a shortage of labour, which easily became acute during epidemic seasons, as, for example, during the plague of 1896–97 or the influenza of 1918–19. During the last 15 years, however, the tide has turned, and to-day perennial factories have passed the saturation point as regards labour absorption and there is increasing unemployment among industrial workers. Labour in the mines and on the plantations is a case apart, and these industries undeniably continue to experience some shortage, especially during particular seasons. It is, however, not likely that, in the near future, there will be any shortage in industrial labour; the rapid additions to the population, the growing impoverishment of the land, the development of communications and the spread of knowledge, the steady improvement in factory conditions, all contribute towards swelling their ranks. Nor, except in a few cases, has the employer now to wander far afield from his factory for collecting his labour force. The smaller industrial centres rely on local and surrounding rural areas for their supplies of labour, and it is only centres like Calcutta, Bombay and Jamshedpur that have to depend on importation. Ratnagiri and the near-by Deccan districts are the recruiting fields for Bombay, while Calcutta depends largely on Bihar, the U. P. and Madras. Jamshedpur also, created as it was out of the virgin forest, depends entirely on outside labour, and the heavy demand due to the rapid expansion of its industry has compelled it to recruit its labour force from almost every Province in India, though, naturally, the vast part comes from the neighbouring Provinces.

While the supply of labour in factories has been ample during the last decade and a half, certain difficulties are still being experienced on the plantations and in the mines. The South Indian plantations do not seem to have suffered

from any dearth of labour, but in Assam and Bengal conditions are different, in that the plantations there have to recruit their workers from far-off areas. Supply of local labour, except to a small extent in the Surma Valley, is negligible, and recruitment has to be carried on in Bengal, Bihar, Orissa, the Central and the United Provinces and Madras. A measure of the difficulty of securing adequate labour supplies for the plantations is the fact that in the year 1934–35—a bad year for the tea industry—18,764 persons were recruited for Assam as "assisted emigrants" and members of their families, at an average recruitment cost per adult of between 80 and 90 rupees. The mines draw on the near-by aboriginal tribes, which are mainly agricultural and therefore easily attracted by the offer of land for cultivation. During recent years the number of non-aboriginal miners has been on the increase, but the supply of labour is still hardly adequate, though partly at least this is due to low wages and inadequate housing accommodation. Workers of this class often return to their villages for their sowing and harvesting, and for their festival seasons. One of the reasons for making the abolition of underground work for women gradual was the necessity to prevent a crisis in the industry by a sudden shortage of labour.

The agricultural bias.—It has been said that the Indian industrial worker is an agriculturist by temperament and a factory employee only by necessity. The Whitley Report has succinctly summarised the attitude of the average industrial worker to the factory by comparing it with that of Englishmen who have come out to India. "The Indian factory worker is in most cases a man who has taken up definite work in a place which he does not regard as his own (in many cases even its language is foreign to him), who cherishes the hope of returning to his country now and then and of retiring there ultimately. He is, as a rule, prepared to abandon the factory if work offering adequate opportunities becomes available in his native place or if the climate makes serious inroads on his health." "Talk of his village," says

Margaret Read, "to a factory worker doing monotonous work among noisy machinery and his face lights up, and though there is sadness and the look of the exile in his face, it is obvious where his heart and most of his thoughts are." The workers' contact with the village is close and constant in a great many cases, while with a few it is more psychological than real. This does not, however, mean that the Indian factory worker is essentially an agriculturist. The number of factory workers who have a direct interest in agriculture is far fewer than is generally supposed, though large numbers of them keep a home and the members of their family in their villages, remit a portion of their wages there and return there periodically to look after their affairs and to obtain rest from the strain of factory life. In the seasonal industries there is an intimate connection between industrial and agricultural work, and in the collieries, too, there is a substantial class directly interested in agriculture. But the perennial factories which offer work throughout the year are now able to command a growing number of employees who form part of the permanent urban population more or less dissociated from the land. In Ahmedabad, for example, full 20 per cent of the working-class population are permanent factory hands, though in other places the proportion may be somewhat smaller. Such contacts with the village, while they exercise an enormous influence on the health and outlook of the worker and provide a sort of unemployment and sickness insurance, and a stay-by in times of strike, have the disadvantage from the industrial point of view of being responsible for the large labour turnover, the low labour efficiency, and the slow progress of unionism. To the important question whether efforts should be directed towards building up an industrial population divorced from the villages or whether the existing contact should be maintained and stimulated, the Whitley Commission has given the categoric reply that the link with the village is a definite asset and should be encouraged and regularised.

III

Labour Efficiency.—Many a hard word has been said about the Indian workers' lack of efficiency. I have elsewhere[1] dealt with Sir Clement Simpson's equation that 2·67 hands in an Indian cotton spinning and weaving mill are equal to one hand in a Lancashire mill, and Sir Alexander McRobert's statement that the English worker is three to four times as efficient as the Indian. Of a piece with this kind of calculation is Sir Hormusji Mody's evidence before the Whitley Commission when he said: "In Japan a weaver minds six looms, and efficiency there is 95 per cent. In China a weaver minds four looms, and efficiency there is 80 per cent. In Bombay a weaver minds two looms, and efficiency is 80 per cent. Calculated on the basis of Japan and China, a weaver in Bombay is paid between 200 and 300 per cent more than a weaver in China or Japan." Commenting on Sir Clement Simpson's estimate, Dr. Gilbert Slater has pointed out that the difference of output was due rather to the greater cheapness of the Indian worker as compared with the British worker, than to inefficiency in the Indian worker. "In Lancashire it is worth while to put only one worker to four looms because you save three workers' wages. But in India the wages are so small that it is not worth while to save that amount at the expense of running the looms at a lower speed, and so the real difference between the efficiency of a Lancashire and a Madras operative is very much over-stated by the ratio of two and two-thirds." On the other hand, Sir Thomas Holland bears testimony to the superior efficiency of the Indian worker. "With Indian labour, you can tackle any industry for which the country is suitable. I have seen labourers at Jamshedpur who only a few years ago were in the jungles of the Santals without any education. They are now handling red-hot steel bars, turning out rails, wheels, and angles of iron as efficiently as you can

[1]See pp. 207–209, 225, 237–239, P.P. Pillai, *Economic Conditions in India*.

get it done by an English labourer." Mr. T. W. Tutwiler, formerly General Manager at Jamshedpur, is of opinion that Indian labour can be trained to replace almost every kind of foreign imported labour.

Effects of Environment.—There is no doubt that, generally speaking, Indian labour is not as efficient as it might be. First of all, unlike industrial workers in other countries, the worker here is brought up in a rural environment, and does not, therefore, possess that keenness of mind and eye enjoyed by those brought up in an industrial atmosphere. That this is a remediable defect is shown by the skill and intelligence of the Bombay and Bengal operatives, which were noted by the Indian Industrial Commission[1] and are obviously due to the fact that these Provinces were the first homes of modern industries in India. Among the general factors which contribute to a lower efficiency is the enervating climate of the country, which creates a strong disinclination to manual labour. The weaker physique and lower vitality of the Indian worker which have caused him to be labelled inefficient have been ascribed by Major Norman White, a former Sanitary Commissioner with the Government of India, as due to removable pathological causes such as malaria, hookworm infection and tuberculosis.[2] Recent experiments have shown that the output of labour which has been treated for hookworm infection has increased by as much as 25 per cent; and this surprising increase in efficiency has been accompanied by a reduction of disease of all kinds. A campaign for better public health and sanitation has therefore to be initiated at once, and that not only in the industrial areas. In the rural regions which are the recruiting centres of labour, we find the same appalling ignorance of the laws of public health. Enquiries made in 1933 by Sir John Megaw, formerly Director General of the Indian Medical Service, showed that (1) India has a poorly nourished population, only 39 per cent of the people being considered fit to be classed as well-nourished;

[1] See p. 18, *Report of the Indian Industrial Commission*, 1918.
[2] Appendix L, *Report of the Indian Industrial Commission*, 1918.

(2) the average span of life is less than half of what it might be; (3) periods of famine or scarcity of food have been occurring in one village out of every five during a ten-year period in which there has been no exceptional failure of the rains; (4) in spite of the excessively high death-rate (22·4 per mille in 1933) the population is increasing (the birth-rate in 1933 was 35·5 per mille) much more rapidly than the output of food and other commodities; (5) motherhood is forced on girls too early in life, the maternal mortality rate is as high as 24·5 per mille, and the infantile mortality rate 170·5 per mille; (6) epidemics of cholera, plague and smallpox are commonplace occurrences, and malaria is constantly present throughout the greater part of India, and (7) worst of all, there is little evidence that the full gravity of the situation has yet been realised. Nor are there sufficient educational facilities for the worker and his children. The Census Report of 1931 shows that the literates per mille aged 5 and over were only 95 in 1931. The late Mr. G. K. Gokhale once suggested that all factories employing not less than 20 children should be compelled to provide for their free education, but the suggestion has found little popularity with the employers. The principle of compulsory primary education still remains unapplied to a large extent, though the experience of the Bombay Municipality in the two labour wards of the city has yielded very encouraging results. The Whitley Report has emphasised that the industrial wards of municipalities have a special claim in the matter of the introduction of compulsory education, and it is to be hoped that the success of the Bombay experiment will inspire other industrial areas also to undertake similar action. It may here be remarked that compulsory education in Bombay stops at 11 years, while the minimum age for factory employment is 12 years, and that the interruption caused by an idly spent year between the ages of 11 and 12 is likely to jeopardise the results already achieved. The I.L.O. is now pleading for raising the minimum age for industrial employment to 15 years, and for a consequent raising of the upper limit for compulsory education; and India also, in order to keep abreast

of the world, will have to advance her age limits in this direction.

One of the special causes which account for the comparative inefficiency of the Indian worker is the unduly long daily period of work. It is true that it has been shortened to nine in the day by the Factories Act of 1934, but even this is too long for a tropical country, and much of the listlessness and "loitering" of which the Indian workman is accused to-day may be explained, in the words of Dr. T. M. Nair, "as a device to reduce the intensity of labour as a safeguard to the worker's physical well-being." The world-demand to-day has advanced from a 48-hour week to a 40-hour week, and recent International Labour Conventions are trying to give effect to this lower limit. It is to be hoped that these circumstances will induce the Government and the employers in India to reconsider the recommendation of the Labour members of the Whitley Commission in favour of a 48-hour week in this country. The level of Indian wages, further, is very low, and does not enable the worker in the lower income-groups to meet even the elementary needs of life, the monthly expenditure on food alone being about 50 per cent of his earnings. At the Washington Textile Conference of 1937, Mr. R. R. Bakhale argued that it is possible to improve wage standards in India without affecting the competitive efficiency of industry, pointing out that the actual labour costs in the Ahmedabad textile industry, where wages are the highest in India, are lower than in the City of Bombay.

Lines of remedial action.—Summing up, the explanation for the present inefficiency of the Indian worker lies not so much in any inherent defects of character as in the nature of his moral and material environment.[1] The Indian Industrial Commission of 1918 observed, and the Whitley Commission has re-emphasised, that the improvement of efficiency depended, *inter alia,* on the following factors: "There is substantial agreement between the best-informed witnesses that the

[1] On this point, see Harold Butler, *Problems of Industry in the East,* p. 22, *et seq.*

remedies for this state of affairs are a rise in the standard of comfort and an improvement in public health. These ends can be attained only by education, improved housing, and a general policy of betterment, in which an organisation for the care of public health must play a prominent part. If the children of workers are provided with education under tolerable conditions of life, a new generation of workers will grow up, who will learn to regard mill work as their fixed occupation. Better housing is a most urgent necessity, especially in the large congested industrial cities. Facilities for health, amusement, shorter hours of work (though a reduction of these may for a time decrease output), and other measures for economic betterment, such as cheap shops for the sale of articles required by the mill-hands, and co-operative societies, are almost equally important. The conditions under which industrial operatives live and work in this country ought, if efficiency be aimed at, to approximate, as nearly as circumstances permit, to those of temperate climates. Continuous factory work in the tropics is, at certain seasons of the year, far more trying than similar work in northern countries. The needs of domestic sanitation in large towns are most pressing. The problem, not only on moral grounds, but also for economic reasons, must be solved with the least avoidable delay, if the existing and future industries of India are to hold their own against the ever-growing competition, which will be still fiercer after the war. No industrial edifice can be permanent, which is built on such unsound foundations as those afforded by Indian Labour under its present conditions." In all these directions, a start has already been made, but how tantalisingly slow is the rate of progress!

IV

Labour legislation.—The earlier attempts of the Government to regulate the conditions of labour by legislation were not always conceived in the interests of the workers. Thus, the earlier Assam Labour Acts, the Workmen's (Disputes) Act of

1860, and the provisions relating to criminal penalties for breach of contract contained in the Indian Penal Code of the same year, were all intended to help the employers and to ensure that they had a docile labour force at their disposal. Protective labour legislation in this country began only some time later, when the growing cotton industry of Bombay began causing anxiety to Lancashire, and the obvious abuses connected with the work of women and children in cotton factories in those days were availed of by Lancashire to insist upon India adopting the Factory Acts of 1881 and 1891. The earlier Act ordained that children between the ages of 7 and 12 should work only 9 hours a day and should have 4 holidays in the month, while the latter Act limited the work of women to 11 hours and of children to 7 hours and protected both classes against night work. As a result of the Berlin Conference of 1890, the first Mines Act was passed in 1901, but it concerned itself mainly with the provision of certain rudimentary safety and sanitary measures. By 1908, owing to the laxity in the administration of the Factory Acts and the absence in them of any legal limitation of the working hours of adult males, working hours had become so intolerably long that two Commissions of enquiry had to make a thorough investigation of the labour conditions prevailing in factories. The Indian Factories Act (XII of 1911) was the first legal attempt to limit adult male working hours, which were not to exceed 12 a day. A compulsory rest interval after 6 hours of continuous work and the reduction of children's hours from 7 to 6 in textile factories were also notable features in the new Act.

The post-war period in India has been an era of progressive labour legislation, and this is not surprising when we consider the new forces that are now at work in this country to accelerate the pace of social reform. One of the outstanding facts from the point of view of labour during this period is the birth of the Indian trade-union movement. The All India Trade Union Congress was founded in 1920, and the Indian Trade Unions Act for the registration and protection of trade unions was passed in 1926. Further,

under the Montagu-Chelmsford Reforms, an attempt was made to meet the desire of labour to be represented in the legislatures of the country. This representation was by nomination, and only a total of 6 nominated seats was first assigned to labour in all the Provincial Legislatures taken together. It is, of course, obvious that the organisation of labour into cohesive units and the bestowal on it of political recognition have contributed to enrich the social legislation of recent times. But perhaps the largest single factor which has determined the course of modern Indian labour legislation has been India's membership of the International Labour Organisation. India's desire to prevent being classed at the International Labour Conference as a backward country in matters of social policy has led to the initiation of many labour measures which might not otherwise have come up for consideration at all. As Mr. C. F. Andrews pointed out in 1928, "the amelioration of labour conditions in India by direct legislation has gone forward more quickly in the last ten years since the I.L.O. was established than was possible in the fifty years before the establishment of the I.L.O. Every one of the great landmarks in Indian labour legislation has been put up since the establishment of the I.L.O. While up to the year 1919 it seemed quite impossible to obtain any more humane conditions with regard to labour in mines, factories and mills, after 1919 every door seemed to be suddenly thrown wide open, and we have been pressing forward from one Act of factory legislation to another." India has so far ratified only 14 Conventions of the I.L.O., but partial action has been taken on several unratified Conventions; and altogether, Geneva has supplied a powerful urge in favour of progressive labour legislation. The growth of Communism among the workers seems also to have effected a sea-change in the Government's outlook on labour problems; and the new dual policy as regards labour seems to consist in the suppression of Communism on the one hand and the removal of the more serious labour grievances on the other. It is thus not perhaps a mere accident that the Meerut Conspiracy arrests preluded the appointment of the Royal

Commission on Labour; anyway, the Recommendations of the Royal Commission, with their guiding principle of the inevitability of gradualness in matters of social reform, have been accepted as the foundation of the Government's labour policy, and have already resulted in an abundant crop of labour measures.

The first of the long series of post-war labour reforms is enshrined in the Indian Factories (Amendment) Act of 1922, which was passed in consequence of the Washington Convention. It was a great improvement on its predecessor in that the number of persons necessary to constitute a "factory" was reduced from 50 to 20, the employment ages of children were raised to 12 minimum and 15 maximum, and no person was allowed to work for more than 60 hours per week or 11 hours per day. The extent to which we have since travelled in this direction on account of the recommendations of the Whitley Commission is indicated by the Indian Factories Act (XXV of 1934), which limits working hours in the case of adults to 54 in the week and 10 a day, gives them a weekly holiday and a rest interval after 6 hours' continuous work, provides for the grant of certificates of fitness for non-adult workers between the ages of 12 and 17, and lays down that no child between 12 and 15 years of age shall work for more than 5 hours a day.

Prompted by the decisions of the International Labour Conference, the Mines Act of 1901 was amended in 1923 by Act IV of 1923, which provides for a weekly holiday, for limitation of hours of adults above ground to 60 weekly and below ground to 54 weekly, and for the prohibition of employment, whether below or above ground, of persons under 13 years of age. Another measure of 1928 regulated shifts and laid down that no person shall be employed in a mine for more than 12 hours a day. In March, 1929, the Government issued administrative regulations to exclude by stages women from work underground, and the exclusion became absolute as from the first October, 1937. Finally, Act V of 1935 limits the hours of work in mines to 54 weekly and 10 daily above ground, and 9 daily below

ground, and raises the minimum age of employment of children in mines from 13 to 15. Consequent upon some serious colliery accidents, further Acts were passed in 1936, 1937 and 1939 with a view to enforcing more stringent measures for safety in mines. It may also be mentioned in this connection that Mines Boards have been established in the more important mining centres for the regulation of general health conditions in these areas.

All the earlier laws regulating recruitment to the plantations, particularly in Assam, were based upon the principle of indenture. That principle has now been definitely abandoned; the provisions relating to indentured labour contained in the Assam Labour and Emigration Act (VI of 1901) were withdrawn by 1915; the various provisions for penal sanctions for breach of contract also disappeared by 1927. Emigration to tea estates is now governed by the Tea Districts Emigrant Labour Act (XXII of 1932) which has given effect to some of the recommendations on the subject made in the Whitley Report, and has thus afforded further protection to the plantation worker.

Transport workers have also benefited from the progressive social legislation of the period. The Indian Railways (Amendment) Act of 1930 attempts to apply to the railwaymen the International Labour Conventions regarding hours of work and weekly rest. As regards maritime workers, the Indian Merchant Shipping (Amendment) Act of 1931 insists on a minimum age for admission of children to employment at sea, and for admission of young persons to employment as trimmers and stokers, provides unemployment indemnity in case of loss or foundering of the ship, ordains medical examination of children and young persons employed at sea, and provides for seamen's articles of agreement to protect their rights. The Indian Ports (Amendment) Acts of 1922 and 1931 prohibit the employment of children under 12 in the handling of goods on the waterside or vessels in ports, and the Indian Dock Labourers Act of 1934 protects dockers against accidents in loading and unloading ships. All these regulations of maritime labour have been the direct result of various International

Labour Conventions, and the ratification by India of the Convention regarding the marking of the weight on heavy packages transported by vessels, regulations to enforce which have been adopted in the "major" ports of India, is also a step in the same direction. While on the subject of labour legislation enacted to protect particular categories of workers, special mention must be made of the Children (Pledging of Labour) Act of 1933, the object of which is to abolish a particularly revolting form of child slavery, and the Employment of Children Acts of 1938 and 1939 which fix an age limit of 15 for children working on the railways and in ports, and of 12 in certain categories of workshops. The Government of the Central Provinces has adopted an "Unregulated Factories Act" in 1937 to regulate the labour of men and women in some of the small establishments not falling within the scope of the Indian Factories Act, and to provide generally for the welfare of labour in such establishments. Maternity Benefit Acts have been adopted by Bombay in 1929, the Central Provinces in 1930, Madras in 1935, and the United Provinces in 1938, and Bengal is now considering similar legislation.

Among the social reform measures of somewhat wider scope adopted during recent times are the Workmen's Compensation Act of 1923, with its various amendments ending with Act XIII of 1939, which guarantees to the worker compensation when he meets with an accident or is stricken by any of the principal industrial diseases; and the Trade Disputes Act of 1929 with its various amendments, and the Bombay Trade Disputes Conciliation Act of 1934 and the Bombay Industrial Disputes Act of 1938, to prevent industrial disputes and devise machinery for conciliation or arbitration. The Land Acquisition (Amendment) Act of 1933 follows a recommendation of the Whitley Commission, and enables an industrial establishment to acquire suitable land for the erection of dwelling houses for the workers. A series of measures has also been adopted to deal with indebtedness, which is an acute problem with the workers. The Bengal Workmen's Protection Act of 1934 and the C.P. Protection of Debtors Act of 1937

seek to prevent money-lenders from besetting industrial establishments, and the C.P. Adjustment and Liquidation of Industrial Debtors Act of 1936 provides a summary procedure for the liquidation of the unsecured debts of workers. In addition, the Code of Civil Procedure has been amended by Acts XXI of 1936 and IX of 1937, to protect honest debtors from detention in a Civil Prison, and to provide that wages below Rs. 100 per month of all workers should be totally exempted from attachment. The Payment of Wages Act of 1936 covers new ground in that it is in the nature of a Truck Act; it seeks to regulate payment of wages to industrial workers so as to prevent the abuse of long delays, and also to limit deductions from wages by way of fines.

Gaps to be filled.—In short, we have here an imposing array of social achievements by way of legislation, most of the major recommendations of the Whitley Commission in this respect having now been given effect to. Much indeed has already been accomplished, but one important gap yet remains. No legislative attempt has so far been made to provide some measure, however feeble, of social security for the workers. In view of the increasing unemployment in industrial areas, a beginning will have to be made not only for the creation of employment exchanges, but also for the establishment of schemes for the relief of the unemployed; and an attempt has also to be made to protect the worker against sickness, old age and invalidity. Besides, the utility of such labour legislation as at present exists has been considerably circumscribed by certain fundamental factors. Criticism has centred round two or three main points. First, how few of the 26 millions of industrial employees have come under the influence of legislative action!—Apart from the extremely limited number of those engaged in organised industry who come under the Mines and Factories Acts, the vast bulk of Indian industrial labour still remains unaffected by the protective measures so far undertaken. The evidence elicited by the Whitley Commission has brought to light the heartless manner in which labour is being exploited in the

numerous industrial establishments which are outside the purview of the Indian Factories Act. By way of illustrating the evils in these unregulated factories, most of which employ large numbers of children well below the regulation age of 12,[1] the Commission refers in some detail to the conditions prevailing in the numerous small factories established in various parts of India for mica-cutting and splitting, wool-cleaning, shellac manufacture, beedi-making, carpet-weaving and leather-tanning, and comment on the "lack of sanitary arrangements and drainage", "the earth space being littered with the evil-smelling refuse and sodden with pools of filthy water," the low wages, the long hours and the absence of holidays. It is heartening to hear that the Government is now investigating the possibility of introducing legislation to remedy the more glaring evils in these unregulated factories.[2] Another difficulty in getting the best possible results out of the existing legislation lies in the ignorance and illiteracy of the worker and his lack of organisation. The Whitley Commission observes that "the Indian factory worker is just beginning to realise the significance for himself of the factory inspector," but complaints made by the workers direct are still extremely few on account of the fear of victimisation by the employer. There is also reason to believe that the benefits conferred by the Workmen's Compensation Act have even now been only imperfectly understood by the working classes, and that in a considerable number of cases the stricken worker either goes without any payment at all or is obliged to satisfy himself with extremely small payments. The Trade Unions Act enables workers' organisations to register themselves and enjoy certain privileges; but the employer is not compelled by law to accord recognition to these unions, nor is the union member guaranteed immunity from dismissal for any active interest he may take in furthering the cause of his organisation. The Trade Disputes Act, though enacted in 1929, had remained practically a dead letter till the

[1] "This has now been partially remedied by Act XV of 1939."
[2] "Some of the Provincial Governments have extended certain provisions of the Indian Factories Act to factories employing less than 20 persons."

introduction of Provincial Autonomy, but attempts are now being made, by the amending Act XVII of 1938 and by provincial legislation on the lines of the Bombay Industrial Disputes Act, to impart greater mobility to conciliation and arbitration machinery.

A word may here be added regarding the general administration of the Factories and Mines Acts. The inspecting services are manned by hard-working and conscientious officials; the standard of enforcement has been steadily rising and the quality of the work has been more than maintained; but they are still too few in number, and in spite of High Court circulars and Government instructions to the contrary, the fines imposed for labour offences still continue to be derisory. Nor is there any specially trained magistracy to deal with labour cases. Further, there is a certain lack of uniformity in the standards of enforcement, for though the Central Government possesses powers of superintendence, direction and control, in practice this has involved no close supervision over administration, which falls within the competence of the Provincial Governments. It is, therefore, necessary that, as in the case of Mines, the responsibility for enforcing the Factories Acts and other pieces of legislation should also be entrusted to the Federal Government. The Rules made by the local governments under the Factories Act are now under the control of the Governor-General-in-Council, and if periodical conferences of the various provincial factory inspectors could be arranged, something will have been done towards ensuring greater uniformity in administration. More vigorous efforts should also be made to ensure that labour laws and administration in the Indian States do not fall short of the standards set up in British India.

V

Trade Unionism.—The Webbs have pointed out that it is not till industrial conditions make it almost impossible for a "worker" to become a "master" that ephemeral combinations of workers can become permanent trade unions. In

India, on account of the worker's nexus with the land, it has been only lately that there has grown up a definite class of workers divorced from all interest in the soil and depending entirely on some form of industrial employment for their sustenance. This may account for the late emergence of trade unionism in this country. It is true that some unions were in existence even before the War, but, generally speaking, labour before the War, apart from some classes of railway and Government servants, had not yet acquired the spirit of combination. There are many instances to show that, while the workers were familiar with the methodology of local strikes and the functioning of strike committees, they were unable to combine over long periods to secure common ends by concerted action. The Madras Labour Union, started in 1918 by Mr. B. P. Wadia, may be regarded as the first conscious attempt at working-class organisation, and the years between 1918 and 1922 witnessed the birth of the more important of the labour unions existing to-day.

There were three main circumstances which favoured the growth of the movement during this period. In the first place, the cost of living in India during these years was steadily rising, and though industry and trade were passing through a period of unprecedented boom and the demand for labour was increasing, wages did not rise proportionately. Secondly, the ferment of the War had awakened labour throughout the world, and in India it evoked a combativeness and a readiness to organise that were previously lacking. A strike epidemic swept through the country during 1918–1922, and the formation of most of the unions of this period either immediately preceded a strike or was the result of its successful termination. A third circumstance which helped the trade-union movement was the establishment of the International Labour Office. The new dignity conferred upon labour by Part XIII of the Treaty of Versailles and the provisions in it for the election of labour delegates to the International Labour Conference on the recommendation of the most representative labour organisation of the country brought about the creation in 1920 of the All-India Trade Union Congress; in the absence

of recommendations from such an all-India body, it was feared that the Government's choice might sometimes fall on persons who did not command the confidence of the working classes. The interest taken by politicians in labour matters has also been mentioned as a circumstance favouring the trade-union movement; but in the presence of other and more powerful causes tending in the same direction, it may be doubted whether the activities of the politician gave anything more than a mere fillip to the movement.

Early in the history of the labour movement in India, the employers resorted to law to challenge the workers' rights of association. The case was eventually withdrawn, but the proceedings suggested that, in the absence of legislation, even legitimate trade-union activity was exposed to danger. This led to Mr. N. M. Joshi's resolution in the Indian Legislative Assembly in March, 1921, urging the adoption of the necessary legislation for the protection of trade unions, though it was only in 1926 that the Trade Unions Act was passed. By the beginning of 1935 there were 213 registered unions, and 183 of these unions had a total membership of 284,918. There were, besides, large numbers of unregistered unions; by the end of the year there were 128 unions in the Bombay Presidency alone with a membership of 111,891, of which only 56, with a membership of 95,506, were registered. While some of these unions exist only on paper, a great many of them have taken permanent root. Transport workers are the best organised, and then come the Government employees.

Special features.—Unionism has progressed rather slowly in India, and it is worth while considering why this has been so. The general tendency here has been to organise by industrial establishments and not by crafts, and the migratory character of the worker and his inability "to stay put" hinder him from becoming rooted in any particular place and to that extent lessen his interest in a trade union. A second difficulty is that union members often belong to different religions and talk different languages, and though the Government has set its face resolutely against

communal developments in trade unionism, the danger is always there. Another reason for the weakness of the movement is that the worker is so exhausted by his long hours in the factory that he hardly possesses the energy to interest himself in anything else for the rest of the day. The prevailing low level of wages is a further impediment to unionism in that the worker finds it difficult to pay his union fee when his wages are hardly sufficient to keep body and soul together. But there are even more fundamental difficulties, such as the absence of the democratic ideal and the lack of education among the workers, which have to be overcome before a healthy trade unionism can develop in this country. It is perhaps due to these difficulties that unionism in India has hitherto remained barren of positive results. The Ahmedabad Textile Labour Association and the unions in one or two public utility undertakings have demonstrated how wide are the range of self-help activities in which labour organisations can usefully interest themselves; and if the generality of unions in the country still persists in the belief that their only function is to conduct strikes and negotiate with the employers, this is as much due to their slender financial resources as to their narrow conception of the possibilities of union initiative.

To add to all these complications, the advent of Communism has introduced internecine strife in the workers' movement. The long-drawn-out textile strike of Bombay in 1928 marked the high flood-level of communistic activities in the country, and though Communism has since waned in influence or else been driven underground, its pernicious effects are still visible. The split in the All India Trades Union Congress in December 1929 was the logical culmination of the divergences of view between those inclined to Communism and the more experienced and responsible labour leaders. A majority of the trade unions broke away from the A.I.T.U.C. at Nagpur to form the Indian Trades Union Federation, and the rump that was left behind was further weakened by a series of schisms among the Communists. Formal unity in the trade-union movement has

now been re-established by the National Trades Union Federation, while maintaining its identity, seeking a temporary affiliation with the A.I.T.U.C. for the pursuit of common interests.

Trade unionism to-day seems to have come to a standstill, not only because of its inherent defects and internal rivalries, but also because of the prolonged economic crisis that set in in 1929 and its inevitable sequel of growing unemployment. Nevertheless, it would be a mistake to assume either that the movement is dead or that it is unsuitable to Indian conditions. Labour unions have a definite function to perform in the changing conditions of Indian industry, and the Whitley Commission has recorded its emphatic opinion that "nothing but a strong trade-union movement will give Indian workmen adequate protection. . . . It is in the power to combine that labour has the only effective safeguard against exploitation and the only lasting security against inhuman conditions." Employers also should find it of advantage to have healthy and representative organisations of employees with which they could deal. In order that the employer may understand the worker's point of view, it is necessary that it should be formulated clearly and authentically. Lasting understanding could be arrived at only between bodies highly organised; negotiations with a mob hardly ever lead to durable results. Indian employers will, therefore, be only studying their own interests in being more generous in "recognising" unions, and in educating themselves out of the feeling that it is beneath their dignity to discuss management problems with representatives of their workers.

VI

Labour and the Constitution.—We may now consider the place of labour in the New Constitution. It has already been mentioned that it was under the Montagu-Chelmsford Scheme that labour was first given some sort of representation in the Legislature. According to the earlier arrangement, only a total of 5

nominated seats was assigned to labour in all the provincial Legislatures taken together, but the number was later on raised to 10, though the method of nomination was still adhered to. No provision was made for labour representation in the Central Legislatures, though Mr. N. M. Joshi, the veteran labour spokesman, has been a nominated member of the Indian Legislative Assembly since 1921. The Government of India Act of 1935 shows a material improvement in this respect; 38 seats have now been allotted to labour in the Provincial Assemblies, of which Madras has 6, Bombay 7, Bengal 8, the U.P. 3, the Punjab 3, Bihar 3, the C.P. and Berar 2, Assam 4, Orissa 1 and Sind 1; and 10 in the Federal Assembly. As against this, however, it is worth while mentioning that employers belonging to the commercial, industrial, mining, planting, and land-holding groups have been allotted 93 seats in the Provincial Assemblies and 18 seats in the Federal Assembly. The effect of the increased workers' representation now granted has thus been nullified by the preponderant influence of the capitalist classes, especially when it is remembered that a great many of the general constituencies would also normally be returning the upholders of vested interests as their representatives to the Legislatures. Further, the recommendation of the Whitley Commission and of the Indian Franchise Committee that labour representatives should preferably be elected by registered trade unions has been considerably watered down by the Delimitation Committee, and labour representation is now divided between trade-union constituencies and "special labour constituencies." The reason for the creation of these "special labour constituencies" was the weakness of the trade unions; and sufficient weight has not been given to the influence which the bestowal of the franchise on trade unions will have on their own development. An analogy is supplied by the International Labour Organisation which laid down that the Government of the Member States should, in nominating the employers' and workers' delegates to the International Labour Conference, take into account the recommendations of the industrial organisations

which are most representative of employers or work-people (Article 389 of the Treaty of Versailles). Such industrial organisations did not exist in a great many countries when Article 389 was framed; but it is common knowledge how the stimulus of the privilege conferred upon such organisations by the Treaty of Versailles soon led to their development and expansion.[1] Likewise, the bestowal of the right of election on trade unions only would have, it seems reasonable to think, led to their becoming a strong and compact agency fitted in every way for the discharge of the responsibilities placed on them.

Representation of labour in the Legislatures is only one aspect of the problem of labour's place in the Constitution. Another aspect relates to the allocation of labour subjects between the Federal and Provincial Legislatures. The Whitley Commission was convinced that "the objections to complete provincialisation of labour were so great that every effort should be directed towards avoiding this course." Its considered opinion was that "legislative powers in respect of labour should continue with the Central Legislature, but Provincial Legislatures also should have power to legislate. Labour legislation undertaken in the Provinces should not be allowed to infringe the legislation of the Centre or its administration." This recommendation was in accordance with existing practice, and has been generally followed in the Act of 1935. The Legislative Lists given in the Seventh Schedule of the Act divide the functions of Government into three catogaries: Federal, Provincial and Concurrent. Factories, the welfare of labour, provident funds, employers' liability and workmen's compensation, health insurance, including invalidity pensions, old-age pensions, unemployment insurance, trade unions and industrial and labour disputes, are placed in the Concurrent List; the regulation of labour and safety in mines and oil-fields occurs in the Federal List; and included in the Provincial List are relief of the poor and unemployment. With the majority of labour subjects in the Concurrent List, this

[1] See pp. 154–160, P. P. Pillai, *India and the International Labour Organisation.*

division seems apparently satisfactory, but one or two questions clamour for reply. What exactly is to be the position of the Indian States in this scheme of things? As it is, the criticism is vociferous that labour standards in the States are far below those in British India and that the tardiness of social reform measures in the former is acting as a brake on progress in the latter. Administration in Indian States being as a rule less responsive to public opinion than in British India, it is too much to expect that the States would on their own initiative attempt to raise their standard of labour-protection to the same level as in British India. In saying this, the praiseworthy efforts that are now being made by some progressive and forward-looking States, notably Mysore, are not overlooked—but one swallow does not make a summer. Nor are the States' nominees to the Central Legislatures, where their voting power will exercise a decisive influence, likely to be enthusiastic in supporting any labour measures on subjects belonging to the Federal or Concurrent List. The States *bloc*, supported by the voting strength of other vested interests, is thus likely to diminish the importance of the Central Legislature in the future as a force making for social justice and equity. The situation seems more hopeful in the Provinces, where, owing to the direct contact between the voter and his representative, the recent extension of the suffrage is bound to have a democratising influence. Secondly, Congress Ministries, pledged to popular programmes, are now in office in 8 Provinces, and even the non-Congress Provinces, in their desire to stand well with the public, are likely to pay more attention than formerly to the needs of the under-dog. As against these factors, it has to be remembered that the new Provincial Ministries will be considerably handicapped in their social programmes by the non-expanding nature of Provincial revenues. Ruthless retrenchment in some directions and the imposition of additional taxation will have to be resorted to, if worth-while social measures, such as even the most modest plans for industrial housing and social insurance, are to be carried out.

It is, of course, difficult to prophesy how things will turn out in the future, but it seems safe to say that the impulse for labour reform will not, as heretofore, come from the Centre, while financial limitations are likely to paralyse Provincial action. Some Provinces may, indeed, initiate plans and policies for the betterment of the workers, but it is obvious that, with industry always migrating to the less protected areas, no Province can afford to embark on far-reaching schemes of this character unless the other Provinces also are willing to keep step with it. On the other hand, it is difficult to see how, in the face of the forces now at work in the country, social ameliorative action can be much delayed. The phenomenal success of the Indian National Congress at the polls has been partly due to its intimate mass contacts, and the Congress scheme of political education is to tell the peasant and the worker what his needs are and how to satisfy them. Close bonds are being created between the Congress, as the main political organisation of the country, and the various economic organisations, as the workers' and peasants' movements. The principles of Socialism are being preached everywhere, and even more radical doctrines than those of Socialism find a place in the mental make-up of the urban worker. We have here a combination of elemental forces which are likely to erupt with violence if legitimate channels for development are denied to them; and statesmen are now beginning to realise that an economic and social policy based on the principles of social justice and equality is after all the best way of forestalling Communism and other disruptive tendencies.

CHAPTER XXIII

COST OF LIVING INDICES AND WAGES

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Importance of real wages.—Price movements were originally recorded to get an idea of probable trade movements and at times quotations for different dates were expressed as ratios of prices on a particular market day. Such price relatives were separately maintained by business firms interested in particular commodities. These price indices were later on applied to measure the changes in the purchasing power of money. Prices of a number of commodities were collected and a simple arithmetic average was computed. The very rapid changes in all countries during and since the War in the prices of the commodities and services entering into the cost of living have made clear the necessity of calculating index numbers showing general changes in that cost, with the special and practical object of using such numbers as means of adjusting various long-term contracts on a money basis to the movement of prices. One of these contracts was the wage contract. The money wages on a particular date were expressed in relation to the purchasing power of money and real wages established. The cost of living index numbers have played an important part in the discussions regarding changes in money wages. Cost of living index numbers have a purely relative character and show the movement in the cost of living over a given period compared to a base period. There is no necessary relation between the items and quantities of the commodities for which prices are obtained and those required to provide a minimum of subsistence or of comfort. They only show price fluctuations. Standards of consumption and nature

of articles differ with region, religion, caste and income. Fluctuations in prices differ with the nature, quality and variety of articles and it is hardly possible to ascertain, at a glance, the general rise or fall in prices. A change in the general level of prices does not necessarily mean, and in practice never does mean, that all prices change at the same rate and in the same direction.

Difficulties in the calculation of price and wage movements.— The task of computing a cost of living index is to find out the average fluctuation in prices of all commodities taken together and their movement from the norm or the base period. It is impossible to include all commodities in an index number, but an effort is made to calculate price movement for most of the important commodities consumed by a majority of men every day. Averaging of the prices of such selected commodities is another step. There are various methods of computing an average. A simple addition of all prices and their division by the number of commodities gives a simple arithmetic average. This average has the drawback of equalising the importance of all commodities and items included in the list. The commodities should therefore be weighted according to their importance. Out of a number of methods of allotting weights the aggregate consumption and the family budget methods are mostly in use. The aggregate consumption method is more suitable for indices calculated for a region or a country as a whole, but when the object is to compare the movement of cost of living indices and wages, or, in other words, to measure the purchasing power of money for a particular class or community, the family budget method is the best.

In India, general index numbers of wholesale prices are published annually, but they are unsuitable for this purpose because the figures are expressed as percentages of the year 1873, because the list of the commodities has not been revised since 1889, and because it includes many commodities which are no longer important and excludes others and is unweighted. It may serve as a record of trade movement but

it is of little value for measuring the purchasing power of money for any community.

With a view to comparing the movement of cost of living and industrial wages in this country, a new index number based on careful estimates of the relative importance of the commodities in the family budget of the Indian industrial labour in various industrial centres is necessary. Finally, an index number computed from the Provincial indices would show the movement of the cost of living for all industrial labour in India.

Since the series of prices of commodities can only include articles which are exactly definable and do not change in their qualities except over long periods the composite index will relate only to food, fuel, rent and simple clothing.

Calculations of the movements of industrial wages are still difficult. It is not possible to obtain authentic published information on any large scale regarding the earnings of the industrial labour, the amount received by an industrial labourer per week or per month. This is due to the too frequent changes in the personnel of factory employees and to the absence of any record maintained by the employers or the newly organised trade unions. The rates of wages payable on different jobs and the estimated average output per day are the only two clues for making a rough estimate of the probable daily income of the different classes of industrial labour. These factors too are most unstable. The rates of wages vary with the type of machinery, the prices of finished goods and the quality of goods produced. Average daily output depends on the personal skill and efficiency of the workers, the continuous supply of raw materials, the pattern and the type of machinery. In spite of the drawback, the rates of wages and average output do give an estimate which is fairly representative of the average income within low percentage of error, and in the absence of more accurate information there appears to be no alternative but to base the comparisons on these estimates. Anyway it can very well show the trend of the movement. Occasional inquiries and reports serve as good

correctives and point out the accuracy or otherwise of such estimates.

A comparison of the cost of living index numbers and the movement of industrial wages on the lines indicated above is undertaken in the following pages.

Calculation of the Cost of Living Index Numbers—On the basis of the retail prices quoted every fortnight in the Provincial Government Gazettes, the prices given in the Reviews of the Trade of India and the Sea Borne Trade Statistics, published by the Director General of Commercial Intelligence, Government of India, the following index numbers of prices for different articles of food have been calculated for the various industrial centres. The basic figure was the average of prices in the quinquennium immediately preceding the Great War, *i.e.*, 1909–13. The adoption of a five-yearly base is intended to remove the abnormality in the basic figure, if any. Moreover, this period was fairly normal from the point of view of price fluctuations.

BOMBAY

(*Base period* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Gram*	*Arhar*	*Jowar*	*Bajra*	*Sugar*	*Ghee*	*Coconut Oil*	*Salt*	*Tea*	*Spices*
1914 .	112	105	113	120	113	113	100	109	117	91	100	105
1915 .	114	129	120	133	100	116	100	105	109	96	113	103
1916 .	118	102	208	135	92	121	123	131	110	100	110	118
1917 .	118	107	125	135	108	126	138	139	111	126	94	118
1918 .	153	164	165	149	229	226	134	131	100	157	94	128
1919 .	155	177	240	224	255	250	190	165	160	135	104	152
1920 .	153	163	213	247	197	184	264	161	184	126	90	131
1921 .	151	175	218	216	205	239	245	153	176	117	98	118
1922 .	178	154	188	210	137	176	208	168	139	130	140	133
1923 .	143	129	143	147	132	145	198	173	140	170	181	157
1924 .	155	130	125	145	137	145	212	170	142	130	187	181
1925 .	149	134	138	139	153	150	188	160	146	143	162	194
1926 .	153	132	155	157	145	161	192	165	140	143	163	182
1927 .	151	136	170	186	150	174	184	160	140	142	171	158
1928 .	159	136	183	198	139	145	182	159	141	122	146	158
1929 .	184	155	200	188	150	171	193	157	136	117	135	175
1930 .	157	118	165	173	142	153	137	158	125	100	127	155
1931 .	84	66	120	120	79	82	152	137	106	117	113	109
1932 .	80	77	110	129	82	89	118	121	106	139	89	108
1933 .	92	86	103	104	89	95	124	95	75	117	113	94
1934 .	80	75	101	107	84	102	134	90	65	119	123	96
1935 .	89	75	92	114	87	93	116	99	68	123	121	92

AHMEDABAD

(*Base year* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Gram*	*Dal Arhar*	*Jowar*	*Bajra*	*Ghi*	*Sugar*	*Til*	*Coco-nut oil*	*Salt*	*Tea*	*Spices*
1914 . .	129	114	134	126	120	126	109	100	112	117	100	100	105
1915 . .	133	129	130	154	117	120	105	100	103	109	100	113	103
1916 . .	148	117	130	166	103	109	131	123	99	110	123	110	118
1917 . .	156	124	133	189	103	86	139	138	103	111	138	94	118
1918 . .	175	179	166	169	200	234	131	134	120	100	134	94	128
1919 . .	208	217	236	194	273	266	165	190	166	160	190	104	152
1920 . .	208	181	239	294	210	189	161	264	239	184	264	90	131
1921 . .	208	205	272	354	260	246	153	245	144	176	245	98	118
1922 . .	183	198	249	277	173	177	168	208	136	139	208	140	133
1923 . .	171	155	193	191	123	160	173	198	138	140	198	181	157
1924 . .	185	152	203	209	143	149	170	212	145	142	212	187	181
1925 . .	185	181	189	229	150	166	160	188	134	146	188	162	194
1926 . .	185	181	196	277	173	186	165	192	141	140	192	163	182
1927 . .	168	152	172	254	160	160	160	184	138	140	184	171	158
1928 . .	167	150	153	246	137	157	159	182	159	141	182	146	158
1929 . .	167	164	206	254	163	186	157	193	154	136	193	135	175
1930 . .	165	121	213	254	140	146	158	137	146	125	137	127	155
1931 . .	52	40	71	77	50	43	137	152	128	106	152	113	109
1932 . .	52	45	80	77	60	49	121	118	148	106	118	89	108
1933 . .	113	105	106	163	97	103	95	124	92	75	124	113	94
1934 . .	100	90	98	149	94	100	90	134	81	65	134	123	96
1935 . .	100	90	107	156	100	102	99	116	91	68	116	121	92

NAGPUR

(*Base period* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Gram*	*Jowar*	*Dal Arhar*	*Ghi*	*Mustard Oil*	*Sugar*	*Salt*	*Spices*	*Chillies*
1914 .	121	123	147	114	166	102	107	100	104	107	94
1915 .	115	137	143	100	142	81	99	100	104	101	117
1916 .	103	117	123	90	132	90	98	123	116	118	117
1917 .	115	123	120	110	134	97	124	138	148	119	114
1918 .	138	177	170	166	171	111	127	134	200	122	156
1919 .	244	243	257	248	303	153	282	190	164	136	231
1920 .	200	240	240	217	303	181	167	264	132	129	140
1921 .	208	246	237	234	261	136	154	245	136	113	141
1922 .	177	220	217	137	192	158	166	208	168	123	185
1923 .	154	151	137	114	158	153	155	198	188	158	167
1924 .	162	166	140	148	174	170	156	212	160	187	149
1925 .	169	189	157	155	153	174	165	188	144	202	158
1926 .	169	189	163	155	211	139	168	192	136	185	167
1927 .	167	186	177	166	224	136	165	184	132	158	156
1928 .	158	164	172	166	210	133	151	182	148	166	120
1929 .	167	187	193	148	203	126	144	193	140	181	144
1930 .	156	129	150	107	171	114	145	137	140	157	144
1931 .	97	83	100	66	121	106	108	152	140	113	88
1932 .	87	94	93	90	108	102	92	118	152	114	77
1933 .	79	97	97	79	100	73	74	124	156	98	73
1934 .	79	87	100	79	103	86	65	134	140	92	117
1935 .	87	87	103	90	110	79	84	116	132	97	68

MADRAS

(*Base year* 1909–1913 = 100)

Year	*Rice*	*Ragi*	*Ghi*	*Til Oil*	*Sugar*	*Salt*	*Other Spices*	*Chillies*
1914 .	104	106	109	112	100	107	107	94
1915 .	96	97	105	103	100	107	101	117
1916 .	105	100	131	99	123	129	118	117
1917 .	104	103	139	103	138	143	119	114
1918 .	122	94	131	120	134	164	122	156
1919 .	167	206	165	166	190	157	136	231
1920 .	162	225	161	239	264	150	129	140
1921 .	149	169	153	144	245	157	113	141
1922 .	140	169	168	136	208	179	123	185
1923 .	140	153	173	138	198	236	158	167
1924 .	151	159	170	145	212	157	187	149
1925 .	165	163	160	134	188	143	202	158
1926 .	149	153	165	141	192	143	185	167
1927 .	156	159	160	138	184	143	158	156
1928 .	162	166	159	159	182	136	166	120
1929 .	149	150	157	154	193	136	181	144
1930 .	127	131	158	146	137	157	157	144
1931 .	87	88	137	128	152	171	113	88
1932 .	87	97	121	148	118	193	114	77
1933 .	80	94	95	92	124	157	98	73
1934 .	63	80	90	81	134	171	92	117
1935 .	69	88	99	91	116	186	97	68

CALCUTTA

(*Base year* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Dal Arhar*	*Ghi*	*Coconut Oil*	*Mustard Oil*	*Sugar*	*Salt*	*Tea*	*Spices*
1914 . .	123	115	130	102	117	107	100	100	100	105
1915 . .	123	190	160	91	109	99	100	129	113	103
1916 . .	126	230	150	99	110	98	123	171	110	118
1917 . .	109	170	133	117	111	124	138	190	94	118
1918 . .	98	173	148	134	100	127	134	186	94	128
1919 . .	142	130	238	149	160	282	190	190	104	152
1920 . .	162	128	250	181	184	167	264	190	90	131
1921 . .	155	173	218	159	176	154	245	190	98	118
1922 . .	153	145	223	171	139	166	208	190	140	133
1923 . .	140	120	195	180	140	155	198	224	181	157
1924 . .	147	108	183	172	142	156	212	238	187	181
1925 . .	155	130	180	152	146	165	188	214	162	194
1926 . .	179	160	188	153	140	168	192	181	163	182
1927 . .	175	160	200	144	140	165	184	181	171	158
1928 . .	168	150	165	143	141	151	182	181	146	158
1929 . .	166	158	215	131	136	144	193	181	135	175
1930 . .	145	100	215	130	125	145	137	167	127	155
1931 . .	70	78	130	118	106	108	152	143	113	109
1932 . .	58	90	120	109	106	92	118	157	89	108
1933 . .	62	93	125	80	75	74	124	148	113	94
1934 . .	64	79	110	82	65	65	134	136	123	96
1935 . .	67	83	113	89	68	84	116	119	121	92

JAMSHEDPUR AND JHARIA

(*Base year* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Gram*	*Dal Arhar*	*Ghi*	*Mustard Oil*	*Sugar*	*Salt*	*Spices*
1914	124	117	134	138	96	107	100	100	105
1915	134	134	141	145	93	99	100	135	103
1916	134	115	122	133	110	98	123	157	118
1917	105	115	116	114	123	124	138	191	118
1918	113	144	144	140	129	127	134	209	128
1919	195	198	228	248	165	282	190	183	152
1920	192	188	209	224	182	167	264	183	131
1921	179	198	206	219	148	154	245	161	118
1922	137	195	206	202	157	166	208	148	133
1923	121	151	259	162	167	155	198	174	157
1924	140	144	134	157	163	156	212	165	181
1925	155	168	150	162	164	165	188	152	194
1926	179	168	166	186	173	168	192	143	182
1927	176	166	178	217	158	165	184	157	158
1928	184	168	191	207	148	151	182	157	158
1929	158	163	194	207	154	144	193	135	175
1930	124	132	125	186	141	145	137	135	155
1931	79	93	109	126	145	108	152	130	109
1932	79	100	103	133	117	92	118	157	108
1933	79	102	103	119	100	74	124	143	94
1934	78	85	100	117	102	65	134	134	96
1935	87	90	108	136	110	84	116	134	92

LUCKNOW

(*Base year* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Gram*	*Dal Arhar*	*Ghi*	*Mustard Oil*	*Raw Sugar*	*Refined Sugar*	*Salt*	*Spices*	*Tea*
1914 .	121	126	148	164	100	107	95	100	100	105	100
1915 .	119	143	148	161	93	99	116	100	100	103	113
1916 .	119	120	116	130	103	98	91	123	129	118	110
1917 .	100	126	108	106	106	124	91	138	143	118	94
1918 .	123	157	156	136	116	127	80	134	176	128	94
1919 .	185	200	276	276	154	282	145	190	143	152	104
1920 .	179	174	216	248	175	167	186	264	152	131	90
1921 .	157	197	248	233	130	154	191	245	143	118	98
1922 .	153	186	196	194	141	166	144	208	133	133	140
1923 .	138	137	108	136	150	155	133	198	176	157	181
1924 .	143	134	108	142	145	156	102	212	147	181	187
1925 .	143	171	148	155	138	165	138	188	124	194	162
1926 .	157	168	164	200	137	168	124	192	124	182	163
1927 .	155	143	168	233	127	165	82	184	124	158	171
1928 .	157	151	192	203	126	151	104	182	124	158	149
1929 .	157	149	192	197	116	144	131	193	129	175	135
1930 .	132	100	100	152	129	145	100	137	138	155	127
1931 .	104	74	88	109	94	108	82	152	124	109	113
1932 .	96	91	96	112	92	92	55	118	133	108	89
1933 .	89	86	100	103	88	74	64	124	133	94	113
1934 .	83	79	92	103	86	65	65	134	133	96	123
1935 .	87	87	96	142	87	84	78	116	133	92	121

CAWNPORE

(*Base year* 1909–1913 = 100)

Year	*Rice*	*Wheat*	*Gram*	*Dal Arhar*	*Mustard Oil*	*Ghi*	*Raw Sugar*	*Refined Sugar*	*Salt*	*Spices*
1914 . .	113	122	163	166	107	120	96	93	100	105
1915 . .	120	138	146	172	99	115	122	107	180	103
1916 . .	128	116	125	147	98	114	113	147	240	118
1917 . .	120	122	125	119	124	120	116	132	270	118
1918 . .	137	154	163	147	127	135	96	209	330	128
1919 . .	174	195	283	306	282	158	151	267	270	152
1920 . .	207	176	221	291	167	197	192	217	310	131
1921 . .	180	203	254	263	154	166	227	287	290	118
1922 . .	167	197	221	197	166	168	178	275	300	133
1923 . .	143	138	121	156	155	188	122	174	360	157
1924 . .	150	138	92	156	156	186	127	161	300	181
1925 . .	161	170	167	169	165	181	156	166	260	194
1926 . .	170	170	184	213	168	171	162	181	250	182
1927 . .	170	149	188	244	165	177	111	191	250	158
1928 . .	172	151	188	234	151	172	118	172	250	158
1929 . .	178	154	233	244	144	170	115	181	250	175
1930 . .	140	100	163	191	145	171	124	244	260	155
1931 . .	98	73	96	141	108	233	89	166	250	109
1932 . .	102	92	96	141	92	144	78	127	250	108
1933 . .	98	89	104	125	74	127	55	164	150	94
1934 . .	87	78	96	122	65	97	78	166	270	96
1935 . .	100	84	100	156	84	100	96	162	270	92

Before calculating the index numbers of the cost of food for various cities, different articles of food have to be weighted. An examination of the family budgets shows a marked difference in the expenditure of labourers according to their incomes. With a view to giving due importance to the variations in the incomes of the labourers, all workers in an industrial centre have been classified into four grades of monthly income, namely, Rs. 15/– and below, between Rs. 15/–and Rs. 30/–, between Rs. 30/–and Rs. 40/–, and between Rs. 40/– and Rs. 50/–; separate weights are allotted to each grade of labourers on the basis of their actual monthly expenditure, and then overall weights are calculated according to the number of labourers in each grade. These weights though they may not be exactly true of any particular labourer or class of labourers, would be fairly representative of the working class as a whole. The following table shows the allotment of weights on the basis mentioned above :—

	Cawnpore	*Calcutta*	*Nagpur*	*Madras*	*Jamshedpur*	*Jharia*	*Ahmedabad*	*Bombay*	*Lucknow*
Rice . .	17·0	54·3	24·3	40·1	50·0	70·0	23·4	51·0	19·8
Wheat . .	42·2	16·9	22·2	—	13·9	2·3	27·8	15·3	37·4
Gram . .	2·0	—	3·6	—	5·6	4·8	3·2	7·3	13·9
Arhardal .	12·0	10·1	10·1	—	8·0	7·5	5·3	2·2	11·5
Jowar . .	—	—	8·7	—	—	—	1·9	8·0	—
Bajri . .	—	—	—	—	—	—	12·0	4·4	—
Ragi . .	—	—	—	42·2	—	—	—	—	—
Sugar (raw) .	1·4	—	—	—	—	—	—	—	1·1
Sugar (refined).	2·6	2·0	7·1	·1	4·8	4·6	3·9	6·6	1·1
Mustard Oil .	6·9	6·0	9·0	—	5·6	4·6	—	—	4·6
Coconut Oil .	—	·3	—	—	—	—	2·0	·38	—
Til or Gingli Oil	—	—	—	6·2	—	—	2·4	—	—
Ghi . .	10·3	4·5	10·0	2·2	6·5	1·4	12·3	1·1	5·4
Salt . .	1·4	1·2	2·0	1·4	1·6	2·5	·6	1·5	1·4
Spices . .	4·2	3·8	1·0	2·9	4·0	2·3	4·4	2·2	3·6
Chillies . .	—	—	2·0	4·9	—	—	—	—	—
Tea . .	—	·9	—	—	—	—	·8	·02	·2

The index numbers of the commodities for various years are now multiplied by the weights allotted to these commodities in each centre respectively and the products of the index numbers and weights are totalled and divided by 100, the sum of all weights.

The following table shows the movement of weighted index number of the cost of food in different centres:—

Year	Bombay	Ahmedabad	Nagpur	Madras	Calcutta	Jamshedpur	Jharia	Cawnpore	Lucknow
1914 . .	110	119	111	105	119	120	122	123	128
1915 . .	115	121	107	99	134	128	161	132	133
1916 . .	121	127	111	104	143	126	130	123	118
1917 . .	118	131	110	106	125	113	112	121	115
1918 . .	163	145	137	113	122	126	122	149	142
1919 . .	180	207	215	186	160	202	203	209	214
1920 . .	173	197	200	191	167	194	196	199	208
1921 . .	174	210	192	156	165	183	183	200	191
1922 . .	172	187	173	155	161	161	152	187	176
1923 . .	145	167	144	149	148	147	139	152	137
1924 . .	151	170	153	156	150	150	147	152	137
1925 . .	150	179	158	163	157	161	159	171	158
1926 . .	153	185	161	152	175	177	178	177	167
1927 . .	164	165	160	156	172	176	178	171	160
1928 . .	157	162	149	161	162	178	182	169	163
1929 . .	175	173	156	151	167	166	164	173	162
1930 . .	148	154	131	133	144	134	135	138	119
1931 . .	90	60	95	94	86	98	92	111	92
1932 . .	88	70	89	98	79	95	90	109	96
1933 . .	93	108	83	88	79	92	88	101	91
1934 . .	87	100	83	77	76	89	86	92	86
1935 . .	90	100	84	82	79	96	94	103	96

Light and Fuel

In calculating the indices for the cost of light and fuel, prices of kerosene oil, castor oil, coke and firewood have to be taken into account. The table below shows the index numbers of prices for these commodities:—

Year	Kerosene Oil	Castor Oil	Coke	Firewood
1914 . .	103	104	87	100
1915 . .	108	96	111	118
1916 . .	125	109	105	94
1917 . .	140	124	109	147
1918 . .	170	157	120	136
1919 . .	178	282	332	142
1920 . .	183	200	190	172
1921 . .	188	156	336	200
1922 . .	178	176	405	142
1923 . .	163	196	249	151
1924 . .	163	220	208	151
1925 . .	163	203	176	158
1926 . .	168	160	204	151
1927 . .	158	159	155	147
1928 . .	135	165	138	151
1929 . .	138	156	133	142
1930 . .	138	147	134	125
1931 . .	133	124	137	113
1932 . .	115	111	138	104
1933 . .	95	103	130	94
1934 . .	93	107	119	79
1935 . .	93	113	91	83

Kerosene oil is generally used by the labourers in all the Provinces though poor class of labourers do use even castor oil which is cheaper. At Jharia the labourers living in the quarters provided by the mine owners get free electric light. Those living outside the settlement in private houses and bustis use kerosene oil.

Firewood is the chief fuel used for cooking in almost all industrial centres in the country with the exception of Jharia, Jamshedpur and Calcutta. At Jharia labourers working in the coal mines get free use of coal, which is supplemented by wood, picked up from neighbouring jungles. At Jamshedpur and Calcutta coal is preferred to firewood due to lower costs.

The following table shows the percentage of expenditure on these items to total expenditure under the group "Light and Fuel." This percentage will serve as weights for calculating the weighted indices for this group.

	Coal	*Firewood*	*Kerosene Oil*	*Castor Oil*	*Total*
Ahmedabad .	2·5	78·2	11·6	7·7	100
Bombay . .	18·3	63·4	18·3	—	100
Jharia . .	—	—	100·0	—	100
Jamshedpur .	72·7	11·4	15·9	—	100
Calcutta . .	57·8	21·1	14·1	7·0	100
Nagpur . .	—	81·25	18·75	—	100
Madras . .	22·2	66·7	11·1	—	100
Cawnpore .	—	78·1	13·6	8·3	100
Lucknow . .	—	69·4	16·7	13·9	100

On the basis of these weights the weighted indices for light and fuel for different centres will be as follows:—

Weighted index numbers for light and fuel

Year	Bombay	Ahmedabad	Nagpur	Madras	Calcutta	Jamshedpur	Jharia	Cawnpore	Lucknow
1914	98	100	100	98	93	91	103	101	101
1915	115	115	115	115	111	110	108	115	113
1916	102	99	100	100	106	107	125	100	101
1917	139	144	146	138	122	118	140	144	143
1918	139	141	146	136	133	130	170	142	145
1919	183	162	152	188	267	286	178	159	168
1920	178	176	177	177	186	173	183	176	178
1921	222	199	198	229	274	297	188	195	192
1922	196	155	152	204	302	339	178	150	153
1923	171	158	156	174	213	224	163	155	161
1924	163	159	156	186	191	194	163	158	164
1925	162	163	162	163	163	172	163	162	167
1926	163	165	160	187	185	192	168	154	157
1927	150	149	155	150	155	155	158	150	152
1928	146	150	151	146	143	139	135	150	150
1929	140	142	144	140	138	135	138	143	133
1930	129	128	112	128	134	134	138	129	130
1931	121	117	117	121	131	134	133	117	118
1932	122	107	106	113	126	131	115	106	107
1933	101	95	94	106	116	120	95	95	96
1934	89	84	82	89	107	200	93	83	85
1935	86	86	85	86	92	90	93	87	89

Clothing

There are wide differences in the dresses of the labourers in different Provinces. The quality, size and variety of cloth change very frequently. It is, therefore, impossible to find out with accuracy the movement in the index numbers of prices of cloth used by the labourers in the various Provinces over long periods. Nor are the records of the price fluctuations for all the varieties of cloths kept and maintained. To get a rough idea of the general trend of prices a few well-known varieties of cloth which are standardised and for which regular quotations are available have been taken into account. The following table gives the index numbers for these varieties of cloth:—

Year	*Imports*			*Exports*			*Average*
	Cotton piece-goods			Cotton piece-goods			
	Grey	White	Coloured	Grey	White	Coloured	
1914 . .	107	106	105	107	84	158	111
1915 . .	100	100	115	93	64	163	106
1916 . .	127	118	150	100	55	142	115
1917 . .	167	153	190	127	61	153	142
1918 . .	240	224	225	187	89	211	196
1919 . .	273	282	290	253	95	242	239
1920 . .	307	312	355	300	139	279	282
1921 . .	247	247	300	280	132	253	243
1922 . .	220	224	255	247	109	253	218
1923 . .	213	218	255	227	86	221	203
1924 . .	227	224	255	207	95	216	204
1925 . .	213	206	220	167	86	211	184
1926 . .	180	188	200	207	89	205	178
1927 . .	167	165	170	200	84	200	164
1928 . .	160	165	175	193	84	195	162
1929 . .	153	171	160	200	82	189	159
1930 . .	133	147	145	167	95	184	145
1931 . .	107	112	115	180	100	168	130
1932 . .	100	106	100	180	66	168	120
1933 . .	87	106	100	167	70	158	115
1934 . .	73	112	85	160	59	153	107
1935 . .	93	112	80	140	48	163	106

House Rent

Workers reside in bustis and labour quarters provided by private landlords, public bodies and the employers. No

regular records are available for the rent paid in the bustis and the quarters provided by private landlords. Workers themselves cannot exactly tell the changes in rent during the whole period of inquiry due to frequent changes of their tenement. At times variations in house rent mentioned by the workers are not very reliable. In many cases, an increase in accommodation or other comforts in a house brings about a rise in rent which, strictly speaking, cannot be treated as an enhancement. It is a compensation for additional comfort. Public bodies at Bombay, Cawnpore and other centres have now devoted their attention to this problem and in some cases have even provided some labour quarters. But they serve no useful purpose for recording the movement in rent in these industrial centres. They are too recent and do not provide a basis for long-term comparison. They are very limited in number and form a very small fraction of the total number of houses necessary for industrial labourers. They are rarely occupied by industrial labour due to a high rental charge—particularly in Bombay. Only the mill settlements are thus left for comparison. House rent does not change from year to year. Compared to pre-war period, there was a rise in rent in 1920–21 when the war conditions caused a general rise in all prices. Since then rent recorded practically no change. In 1929–30, there was again a rise, and these rates continue up to this day. There might have been minor changes now and then, but they do not vitiate the general trend. Due to the regulations of Bombay Rent Act of 1918, the house rent at Bombay could not go up very high.

The following table shows the index numbers for rent:—

Year	Bombay	Ahmedabad	Madras	Nagpur	Calcutta	Jharia	Jamshedpur	Cawnpore	Lucknow
1914 . .	100	100	100	100	100	—	100	200	100
1915 . .	100	100	100	100	100	—	100	200	100
1916 . .	100	100	100	100	100	—	100	200	100
1917 . .	100	100	100	100	100	—	100	200	100
1918 . .	100	100	100	100	100	—	100	200	100
1919 . .	100	100	100	100	100	—	100	200	100
1920 . .	132	292	200	200	200	—	100	200	200
1921 . .	132	292	200	200	200	—	100	200	200
1922 . .	132	292	200	200	200	—	100	200	200
1923 . .	132	292	200	200	200	—	100	200	200
1924 . .	132	292	200	300	200	—	100	200	200
1925 . .	132	292	200	300	200	—	100	200	200
1926 . .	132	292	200	300	200	—	100	200	200
1927 . .	172	359	200	300	300	—	100	381	250
1928 . .	172	359	200	300	300	—	100	381	250
1929 . .	172	359	200	300	300	—	100	381	250
1930 . .	172	359	200	300	300	—	100	381	250
1931 . .	172	403	200	300	300	—	100	381	250
1932 . .	172	403	200	300	300	—	100	381	250
1933 . .	172	403	200	300	300	—	100	381	250
1934 . .	172	403	200	300	300	—	100	381	250
1935 . .	172	403	200	300	300	—	100	381	250

Miscellaneous

There are a number of miscellaneous expenses incurred by the labourers every month. Items included under this head are: Barber, dhobi, sweeper, medicines, education, railway fares, tobacco, liquor, toddy, pan supari (betel nuts), amusements, festivals, remittances abroad, interest on debt, repayment of debt, subscription, etc. The most common and more or less permanent miscellaneous expenditure is on smoking and on the use of finely-cut betel nuts for chewing. Tobacco leaf mixed with lime and betel nut chips is the commonest form of the use of tobacco, though indigenous smoking pipe known as huqqah (an Indian apparatus for smoking) and biris (inferior type of country-made cigarettes; the tobacco leaf chips are wrapped up in a piece of dried leaf instead of paper) are also used. Cigarettes are less popular due to high costs. No regular records of the cost of other services and articles, which are casually used, are available and they have been ignored in the present enquiry. The index numbers for betel nut and tobacco leaf are given overleaf:—

Year	Betel nut	Tobacco Leaf			
		Bombay, Ahmedabad, Madras, Calcutta and Lucknow	*Jamshedpur and Jharia*	*Nagpur*	*Cawnpore*
1914 .	180	112	66	95	143
1915 .	181	112	66	97	110
1916 .	90	112	73	107	107
1917 .	89	138	76	110	132
1918 .	97	138	79	116	155
1919 .	111	215	66	131	131
1920 .	123	224	89	158	146
1921 .	113	233	155	141	162
1922 .	119	276	158	146	188
1923 .	118	250	231	140	161
1924 .	129	241	195	152	149
1925 .	154	250	198	127	180
1926 .	171	276	102	124	202
1927 .	168	293	386	140	211
1928 .	142	319	429	149	171
1929 .	134	336	528	188	186
1930 .	132	310	426	103	158
1931 .	111	276	488	91	118
1932 .	91	284	475	92	68
1933 .	74	276	130	90	49
1934 .	66	250	145	95	56
1935 .	61	276	144	87	76

Betel nuts and tobacco are equally important and hence equal weights are allotted to them. Thus the weighted index number for the cost of miscellaneous items would be as follows:—

Year	*Bombay, Ahmedabad, Madras, Calcutta and Lucknow*	*Jamshedpur and Jharia*	*Nagpur*	*Cawnpore*
1914 .	146	123	138	162
1915 .	146	124	139	146
1916 .	101	82	99	99
1917 .	114	83	100	111
1918 .	118	88	107	126
1919 .	163	89	121	121
1920 .	174	106	191	135
1921 .	173	134	127	138
1922 .	198	139	133	154
1923 .	184	175	129	140
1924 .	185	162	241	239
1925 .	202	176	241	167
1926 .	224	137	148	186
1927 .	231	277	154	190
1928 .	231	286	146	157
1929 .	235	326	161	160
1930 .	221	279	118	145
1931 .	194	300	151	115
1932 .	188	283	92	80
1933 .	175	102	82	62
1934 .	158	106	81	61
1935 .	169	103	74	69

General Cost of Living Index

A weighted general cost of living index number is now calculated by multiplying these weighted indices for separate groups in each centre by weights for each group at that centre in the total expenditure in all groups and divided by the total number of weights for all groups. The following table shows the weights (on the basis of the numerical strength of the different grades of labourers) for each group of expenditure in different centres:—

	Bombay	*Ahmedabad*	*Nagpur*	*Madras*	*Calcutta*	*Jamshedpur*	*Jharia*	*Cawnpore*	*Lucknow*
Food . .	54·1	57·3	58·8	60·6	65·4	60·0	76·0	48·2	52·0
Light and fuel .	7·7	7·5	6·9	7·5	7·2	11·0	·5	6·2	7·5
Clothing . .	7·0	9·3	8·1	3·9	7·5	9·0	8·0	7·6	
Rent . .	12·4	12·8	4·1	8·1	4·9	8·0	—	9·0	7·0
Miscellaneous .	4·8	·9	3·1	·02	·9	1·0	1·0	2·4	1·1
Total .	86·0	87·8	81·0	80·12	85·9	89·0	85·5	73·4	75·7

The following table shows the weighted general cost of living index numbers for all centres:—

Year	Bombay	Ahmedabad	Nagpur	Madras	Calcutta	Jamshedpur	Jharia	Cawnpore	Lucknow
1914 . .	110	114	111	104	115	114	121	131	121
1915 . .	114	116	108	101	128	121	155	137	124
1916 . .	116	119	109	104	135	120	126	129	108
1917 . .	119	130	113	110	125	122	115	135	109
1918 . .	152	144	143	117	128	131	129	159	139
1919 . .	173	191	203	168	173	206	205	204	200
1920 . .	177	218	206	195	181	191	191	204	212
1921 . .	178	224	196	184	183	194	188	202	197
1922 . .	174	203	176	167	169	183	193	188	181
1923 . .	152	188	152	159	162	158	196	164	153
1924 . .	156	191	165	160	161	157	153	167	153
1925 . .	154	195	168	168	151	159	197	175	166
1926 . .	157	198	169	161	178	171	178	188	171
1927 . .	168	194	168	160	187	167	178	182	169
1928 . .	163	190	158	164	169	166	181	165	171
1929 . .	175	198	163	155	172	157	164	204	169
1930 . .	154	182	139	140	153	133	138	169	137
1931 . .	114	135	113	109	107	108	98	147	115
1932 . .	100	128	109	111	101	105	95	143	115
1933 . .	112	151	98	102	99	99	91	135	110
1934 . .	105	144	96	92	95	106	88	127	104
1935 . .	107	144	97	96	96	97	95	135	112

Wages

Wages vary from Province to Province, industry to industry, and job to job. No reliable statistics about the wages of industrial labourers are available. The Government of India publication, *Prices and Wages*, recorded the wages paid by a few industrial concerns for most of the jobs in an industry in the different Provinces of the country. For two reasons these figures do not depict the true state of affairs. Firstly, the classification of labourers in all the departments of an industry is not uniform. In many cases wages are quoted only for males, females and children. Secondly, in arriving at the average monthly wage of a worker in a particular department, the monthly paysheet of the factory for that department was divided by the number of employees in the department. It was only a simple arithmetic average affected by the high wage of a mistry and the very low wage of an unskilled labourer. The publication, however, was given up in 1923. Since then annual reports of the working of the Indian Factories Act in the various Provinces recorded the Provincial average of the wage rates for a few selected jobs. The data supplied by these reports are very meagre and undependable. The wages for a few jobs are quoted even without mentioning the name of the industry and the nature of work, *e.g.*, a fitter or an engine driver in a big factory gets more than Rs. 100/- a month and a fitter or an engine driver in a small repairing shop earns about Rs. 20 to Rs. 25 a month. In the reports both of them are totalled together and divided by 2. Secondly, the figures are the simple arithmetic averages of the wages paid by all the employers in the Province, who submit the returns for different departments of their mills. In the United Provinces even these figures have been discontinued from 1928. No definite information is available about the number of employees working on various rates, and without this, reliable average rates cannot be obtained even for men on monthly rates of pay; while the piece-wage system practised in the various industries and Provinces is very

complicated. It is therefore difficult to arrive at piece-work earnings which can be generally accepted as correct.

Variations in wages may be due to the changes in the type of machinery in use. A simple rise or fall in the piece rate or time wage cannot therefore be taken as an index of a rising or falling income. The high rate may be due to higher skill necessary for working improved types of machines or it may be due to reduced output per hour. In textile mills, the substitution of fine counts for coarse ones or a change in designs may necessitate changes in wage rates which may affect the daily earnings.

Subject to these limitations, and from whatever material is available from official publications, official or non-official inquiries and reports and personal investigations, a rough estimate of the workers' income in various industries is attempted. At Bombay the average monthly wage of a weaver, a spinner and an unskilled coolie in 1913–14 was about Rs. 25, 20 and 12 respectively. These rates remained more or less stationary till 1917. On January 1, 1918, due to rising cost of living and high profits, a general increase of 15 per cent was given to all the workers. A year later another increment of 20 per cent was granted. The third increment came in 1920 which raised the wages of the time wage earners by another 20 per cent and those of the piece wage earners by 40 per cent. The total rise by 1920 was thus 55 per cent and 75 per cent for time and piece-rate workers respectively. Yet another increment was given in 1921, bringing the total rise in wages of time and piece workers to 70 and 80 per cent respectively. In addition to this, there was a separate dearness allowance at a flat rate of Rs. 2 for 32 days, *i.e.*, one anna per day. Wages during 1922 and 1923 remained stationary. In 1923 an attempt was made to reduce wages, but it resulted in a serious labour strike. The wages could not be directly reduced till 1926 though during this period some deductions were indirectly effected. Between 1926 and 1928 the wages again remained stationary with the only change that the dearness allowance was either stopped or added to the regular wage rates. There has been a reduction in wages

between 1926 and 1934, the average fall up to 1933 being 17 per cent. It was raised to 21 per cent in 1934.

At Ahmedabad the average monthly wages of a weaver, a spinner and an unskilled coolie were about Rs. 20, 11, and 10 respectively. Wages rose between 1918 and 1921 when the average monthly income for weavers, spinners and unskilled coolies were Rs. 44, 25 and 18, showing a rise of 120, 127 and 80 per cent respectively. In 1923, wages were reduced by 15 per cent of the then current rates of wages, bringing down the actual rise in wages, compared to 1914, to 87, 93 and 53 per cent respectively. Wages were increased again in 1929 by 8 per cent and 5 per cent for spinners and weavers respectively, but this was neutralised by the cut of 6¼ per cent imposed from January, 1935.

At Nagpur, the average monthly wages for a weaver, spinner and an unskilled coolie were Rs. 19, 8, and 9 respectively. In 1918 the wages were raised to Rs. 21, 10/8/–, and 11. The next increment was given in 1920, when the wages were Rs. 31, 14 and 16, a total rise of 70, 75 and 78 per cent respectively over the wages paid in 1913 and 1914. In 1924 wages rose to Rs. 36, 16/8, and 18. From 1924 the wages remained stationary with a tendency to fall. In 1929 the monthly wages of a weaver, spinner and coolie came down to Rs. 33, 16 and 15. During the depression period between 1929 and 1935 the fall has been very steep, the wages being reduced to the lower rates of Rs. 26, 15 and 11, a reduction of 22·2, 6·25 and 27 per cent respectively.

At Madras, average monthly wages for a weaver, spinner and a coolie were about Rs. 13, 9/8, and 9 respectively. During the War the rates of wages gradually rose till they were Rs. 21/8, 16/4 and 16/8 in 1921. The increase continued till 1923 when the wages reached the maximum amounts of Rs. 26, 18 and 17. Between 1923 and 1929 the wage rates did not show marked variations, though a downward trend was always noticeable. In 1930 there was again a slight rise in wages when the wage of a weaver and spinner surpassed even the old rates of 1923, though

with a very narrow margin. The rates in 1930 were Rs. 27/8, 20 and 13/4 respectively. During the depression the wages came down and reached the low level of Rs. 23, 15 and 10/8 in 1934 and 1935.

At Calcutta approximate average monthly wages in a cotton mill and a jute mill for weavers, spinners and coolies in 1914 were Rs. 22, 14 and 10. Slight rise in wages continued throughout the war period which was followed by a general and substantial increase in 1920 when the rates were Rs. 35, 17/8 and 15, a rise of 59, 25 and 30 per cent respectively. In 1921, wages further rose to Rs. 37, 20 and 17. By 1927 these rates came down to Rs. 30/2, 16/1 and 12/15. When the Indian Jute Mills curtailed production to a four-day week the workers were granted an additional allowance to compensate for the loss in wages, known as khorāki (meals) payment, which was practically equal to another day's pay. The khorāki payment was first paid in December, 1918, and was continued till December, 1919, when it was stopped owing to mills resuming full working days in the week. Since 1921 this payment was resumed and has now been incorporated in the wage rates. From 1921 to 1930 wages continued to fall, though the reduction was not very steep. In 1930 the wages were Rs. 28/4, 14/13/6 and 11/8. The general reduction in wages began in 1931 when the wages came down to Rs. 22/8, 15 and 11. These rates continue till to-day.

At Cawnpore and Lucknow approximate average monthly wages of a weaver, spinner and a coolie were Rs. 12, 18 and 6 respectively in the pre-war year 1913. From 1915 wages showed a gradual rise year after year up to 1922 when the maximum rates of Rs. 36, 28 and 17 were touched. The phenomenal increase in the wages of a weaver was due to the double-loom, and at times even three-loom, system, followed in the cotton mills in preference to the old practice of working on single-loom weaving system. From 1922 to 1925 was a period of gradual fall in wages. In 1925 there was again a slight rise in wages compared to the previous year, though on the whole wages were considerably below the 1922 level. In 1929 the wages had

come down to Rs. 25, 18/8 and 15. In 1931 there was a marked reduction in wages by 24, 19 and 7·5 per cent and this fall continued till to-day.

In the collieries at Jharia the rate of wages per tub of coal raised by a miner was 4½ annas. It was raised to 6 annas at the beginning of the war and subsequently increased to 8 annas per tub in 1916. Between 1923 and 1930 there was a continuous but slow decrease in wage rates. The rates of annas 7·6, 6·4, 6·0, 5·8, 5·5, 5·4 and 5·3 per tub were paid during the period of seven years from 1924 to 1930. In 1931, 1932 and 1933 the fall was very appreciable, the rates being 4·7, 3·6, and 3·2. The last rate continues up to the present day. Thus in 1931, 1932 and 1933 the index number for wages compared to pre-war rates was 104, 80 and 71.

At Jamshedpur the first increase of 10 per cent in wages was given in 1917 due to increased cost of living. In 1920, after the big strike in the Tata Works the index number for wages rose to 140. In 1922 the Iron and Steel company wanted to reduce wages by 10 per cent, but due to the second strike it could not be given effect to. In 1927 and 1928 there was a fall in wages by 2 per cent. The third strike came in 1928 when wages were raised again. In 1929 wages were increased by 17 per cent over 1926 rates. The total increase compared to pre-war days was 64 per cent. These rates are paid till now.

The table on the opposite page compares the movement of the cost of living and wage indices in these industrial centres during the whole period of the inquiry:—

An examination of the table shows that almost in every case between 1914 and 1920 the cost of living index was much higher than the wage index except at Jharia where an immediate increment in wages was allowed at the outbreak of the War. As a result of this disparity between the income and the expenditure of the industrial labourers during the war period when prices were violently rising, a general rise in wages was granted in 1921 and 1922. At Bombay, Nagpur, Cawnpore and Lucknow the revised wage rates covered the increased expenses of living, while

Year	Bombay		Ahmedabad		Madras		Nagpur		Calcutta		Jharia		Jamshedpur		Cawnpore		Lucknow	
	C[1]	W[2]	C	W	C	W	C	W	C	W	C	W	C	W	C	W	C	W
1914 . .	110	92	114	95	104	116	111	100	115	101	121	130	114	100	131	117	121	117
1915 . .	114	115	116	102	101	116	108	100	128	101	155	130	121	100	137	118	124	118
1916 . .	116	115	119	100	104	142	109	100	135	102	126	178	120	100	129	112	108	112
1917 . .	119	115	130	112	110	130	113	100	125	105	115	178	122	110	135	139	109	139
1918 . .	152	115	144	135	117	142	143	118	128	102	129	178	131	110	159	154	139	154
1919 . .	173	135	191	168	168	142	203	118	173	116	205	178	206	110	204	179	200	179
1920 . .	177	165	218	207	195	142	206	174	181	138	191	178	191	140	204	217	212	217
1921 . .	178	182	224	209	184	169	196	172	183	154	188	178	194	140	202	222	197	222
1922 . .	174	182	203	209	167	169	176	175	169	154	193	178	183	140	188	233	181	233
1923 . .	152	182	188	178	159	200	152	178	162	154	196	178	158	140	164	210	153	210
1924 . .	156	182	191	178	160	200	165	196	161	154	153	170	157	140	167	216	153	216
1925 . .	154	182	195	178	168	210	168	196	151	154	197	142	159	140	175	217	166	217
1926 . .	157	185	198	178	161	192	169	175	178	154	178	130	171	140	188	221	171	221
1927 . .	168	185	194	178	160	192	168	169	178	129	178	129	167	138	182	206	169	206
1928 . .	163	185	190	178	164	196	158	172	169	129	181	122	166	138	165	209	171	209
1929 . .	175	185	198	190	155	171	163	177	172	129	164	120	157	164	204	174	169	174
1930 . .	154	185	182	190	140	225	139	169	153	120	138	118	133	164	169	174	137	174
1931 . .	114	185	135	190	109	171	113	167	107	107	98	104	108	164	147	146	115	146
1932 . .	100	185	128	190	111	171	109	172	101	107	95	80	105	164	143	146	115	146
1933 . .	112	168	151	190	102	171	98	158	99	107	91	71	99	164	135	146	110	146
1934 . .	105	163	144	190	92	145	96	142	95	107	88	71	106	164	127	146	104	146
1935 . .	107	163	144	178	96	145	97	142	96	107	95	71	97	164	135	146	112	146

[1] Cost of living index number.
[2] Wage indices.

at Ahmedabad, Calcutta, Madras and Jamshedpur even the increased wages remained considerably below the cost of living. At Jharia no further increment was given at this time even though the cost of living had surpassed the increased rate of wages paid during the war period. The transition period between the war boom and the economic depression showed a downward tendency both in prices and wages. During the period 1923 to 1928, with the exception of Ahmedabad, Calcutta, Jharia and Jamshedpur where the wage indices were lower than the cost of living indices, other centres showed a small margin of wages over the cost of living. In the depression period, however, there were steep falls both in the indices of wages and cost of living—this time the expenses falling below the wages. The solitary exception to this general tendency was presented by Jharia where wage reductions exceeded the fall in the price level.

The low cost of living index during the depression years was due to the fact that the groups included in the family budget showed a high proportion of expenses on cereals which had the record fall in prices. The various services that could not be included for recording price changes remained as costly as before and with a provision for the increased expenses for these services the small margin of excess would vanish.

The excess of wage indices over cost of living indices should not be taken to mean that the workers are well off and should remain contented with the amount they are at present earning. This essay only shows the comparative rise or fall in both these factors and their disparity. The fact remains that the standard of living of the industrial labourers in India is in no case better than semi-starvation standard and needs immediate attention from all interested in the welfare of the labourers and the industries wherein they are employed and the country in general.

CHAPTER XXIV

INDIAN EMIGRATION

By Radhakamal Mukerjee

Trends of Asiatic emigration.—In the south and east of Asia more than half the human race is now confined to an area which represents only 4 per cent of the globe surface. On the opposite shores of the Pacific and Indian oceans are vast, manless areas to which "the flowing myriads from the East" seek admission. The outward thrust of the Chinese, Japanese and Indian emigrants to the undeveloped monsoon, equatorial and cold temperate lands within Asia is one of the most outstanding, yet neglected, economic phenomena in this continent during the last few decades. In the entire Indo-Pacific region there is an enormous disparity of population pressure and standard of living, which invites a constant flow of migrants from the densely to the thinly inhabited areas. In this as well as in the exclusive national or regional policy of Oriental exclusion we have the seeds of a momentous issue which may involve the civilised races in a world conflict. Among the three Oriental countries, the population pressure is higher in Japan and China than in India. India's industrial resources, though limited as compared with Western Europe and the United States, must be considered larger and more varied than in Japan. Thus a rapid industrialisation may afford an outlet for her teeming millions. Yet over-population and the desire for a higher standard of living are responsible for an annual emigration of about 200,000 persons from the Indian shores. The total number of Indians now settled abroad is about 4,125,000, of which only 186,000 are outside the British

Empire.[1] About 1,910,000 Japanese reside outside Japan proper, only 762,500 Japanese living outside their own empire, but the Chinese far outnumber the Indian or Japanese colonists. The number of Chinese now living abroad is 8,180,000 according to Ta Chen.[2] In spite of Oriental exclusion the total number of Orientals now settled abroad is about 16 million persons (*vide* Appendix). On account mainly of the economic depression and to some extent due to restrictive measures adopted by the old immigration countries, continental emigration in Asia has received a serious setback. The number of Indian emigrants, for instance, which rose from 214,805 in 1926 to 221,767 in 1927 declined to 109,561 in 1928; it rose again to 137,910 in 1929, but dropped to 31,720 and 10,043 only in 1931 and 1933. In 1934, however, the figure went up to 130,194, giving distinct proof of a renewed movement. On the other hand, the number of immigrants steadily rose from 89,772 in 1927 to 134,453 in 1929 and 164,052 in 1930. In 1933 the immigration figure fell to 111,232. Similarly, the number of Chinese emigrants (through Hong Kong) which rose from 216,527 in 1926 to 285,593 in 1927 declined steadily to 257,162 in 1928, 227,523 in 1929, 188,900 in 1930, 100,869 in 1931 and 55,639 in 1932. In 1933 the figure rose to 57,515. In these three years the number of returned emigrants was also on the increase, the figures being 187,847 (1928), 185,390 (1929), 223,136 (1930), and 283,890 (1931). The recent years show, however, a diminution, the figures being 232,396 in 1932, and 141,133 in 1933.[3] In Burma alone the total number of immigrants declined from 368,590 to 309,426, while there was also a heavy fall of emigrants from 399,276 to 367,121 between 1930 and 1931. The lowest figure of emigrants (141,133) was reached in 1933.[4] In 1934 the total number of immigrants was 256,004 and of emigrants 226,698.

[1] The official estimate is 2,404,000, but this excludes Burma and many small settlements. *Vide Census Report of India*, 1931, p. 72.

[2] Chinese Consular Statistics give 10,000,000 as an approximation.

[3] Statistics of Emigration and Immigration, *International Labour Review*, January, 1933.

[4] Burma Administration Reports.

Similarly the emigration to Ceylon and Malaya heavily declined as shown below[1]:—

Number of Emigrants from Indian Ports to

	1929–30	1930–31	1931–32	1932–33	1933–34	1934–35	1935–36	1936–37
Ceylon	58,201	43,535	30,856	17,136	18,692	80,840	8,872	7,005
Malaya	76,999	31,210	5	1	19	29,789	4,710	5,501

The economic depression which began in 1930 resulted in the reduction of wages and repatriation of Indian estate labourers in Ceylon and Malaya. Only in the course of five months in 1930 as many as 73,000 Indian labourers were repatriated from Malaya. The same year saw the complete cessation of recruitment from India to Malaya and to the rubber estates in Ceylon. With the rise of rubber prices and revival of work on estates, however, a shortage of labour was felt in the subsequent years. In 1933 the Government of India, on the request of the Malayan Government, permitted the reopening of voluntary assisted emigration. This was, however, restricted to 20,000 during the first year (1934) and was regulated by a quota system subject to certain safeguards. The flow of emigration revived temporarily, the labour requirements being met in 1935 by assisted recruitment of 13,267 emigrants and 7,545 non-emigrants. This system was, however, discontinued in 1936 when voluntary assisted emigration was allowed without a quota. In 1936 the number of assisted emigrants and labourers was 27,858, but this increased to 104,979 in 1937. The total number of Indian labourers in Malaya at the end of 1937 was 355,343 as compared with 290,395 at the end of 1936. Obviously the supply of labour exceeded the demand. This explains why the living wage of the plantation worker is still exceedingly low. The employers aim at maintaining a surplus so that in case of early revival of the rubber industry the scale of wages does not show a sharp rise. Besides the low scale of wages another important drawback is the

[1] *Statistical Abstract of British India*, 1935.

disparity between the proportion of men and women emigrants. Such disparity cannot be remedied unless the Malayan Governments systematically encourage the labourers in settling on the land. And in fact the Indian Government should now permit assisted emigration only in so far as prospects of land settlement are held out for the emigrants. The year 1936 already saw a good deal of labour unrest. Following the recommendation of an Indian deputation led by Sastri the Malayan Government in 1937 restored the wages of Indian labourers to the level at which they stood prior to 1930. But the fresh decline of rubber prices since the end of 1937 led to the reduction in wages on rubber estates. This has eventually led to the prohibition of all assisted emigration to Malaya until supply and demand approach equilibrium.

Of the total population of Ceylon amounting to 5½ millions, over 7 lakhs are Indians, approximately one-eighth of the population. The emigration of Indian labour to Ceylon greatly declined as the result of the economic depression, as will appear from the table above, but the demand for labour revived with improvement in rubber and tea industries. In 1934 the total number of arrivals of estate labourers in Ceylon was 140,607 and the departures 54,790, a net increase of 85,817. In 1935, however, the arrivals were reduced to 8,795 only, as after the large recoupment in 1934 the estates found their labour forces practically sufficient. In 1937 the Ceylon Government approached the Government of India for permitting the recruitment of 5,000 labourers. But the latter withheld permission as neither any revision of wages was promised nor was any assurance forthcoming from Ceylon regarding the extension of franchise to the Indian estate labourers. According to the Village Communities Ordinance, which was passed by the legislature in Ceylon in 1937, the franchise is given to persons owning not less than 5 acres of land in a village area on which the land tax is payable. This has practically excluded the bulk of the Indian estate labourers, who had little opportunity of acquiring land even of that size. In 1938 an Emigration Bill was passed by the Central Legisla-

ture in India which seeks to control "unassisted" emigration, the latter having contributed to depress the conditions of labourers, Indian and others, in various overseas countries where Indian emigration is still permitted.

The Indians as pioneer farmers and settlers.—Oriental migrants have gone to most pioneer belts in the world that needed an industrious population, and have undertaken reclamatory or extractive work invaluable for new communities. At the early stages they were brought into the new areas usually by a system of indenture or contract and offer of facilities of settlement on the land, sometimes including free passage, free housing, medical attendance and free pasture for cattle, as in the West Indies. But later free migration followed the old routes of contract labour. The origin of the overseas Asiatic settlement accordingly was mostly released indentured labour, or labour originally invited and recruited for the development of pioneer lands. The Indians have thus gone in large numbers to the plantations of Ceylon, where they number 1,113,000, and to the mines and plantations of Malaya, where they are 624,000. Indian emigration to these adjacent regions is governed largely by the conditions of rainfall and harvest on the Indian continent. Therefore emigration had, and still has, its recurrent periods of progress and setback corresponding to agricultural prosperity and depression in India. On the other hand, emigration to distant colonies was followed by a tendency towards permanent settlement.

This tendency, specially marked since the abolition of indentured labour in 1922, has been offset, however, particularly in regions where the resident Indian emigrants are dominant in agriculture, commerce and the professions, by the use of political power as an engine of economic oppression of the Indian competitors. In Mauritius, which is the half-way house between Asia and Africa, Indian settlement began from 1839 under a system of indentured labour when the abolition of slavery threatened the ruin of the sugar estates, and now the Indians number 281,000,

representing more than two-thirds of the entire population, and possess about 40 per cent of the cultivated area. The colonising pioneers saved the island from financial ruin as it also saved Natal later, and the Indo-Mauritians are responsible to-day for the island's encouraging agricultural and commercial position as one of the highly productive areas in the British Empire, notwithstanding the visitations of cyclones, droughts and epidemics and the present depression. The first shipment of Indian labour reached Natal in 1860 in aid of pioneer enterprises on coast lands. In 1936 the Indian population here increased to 183,646. Outside Natal the position of the Indians in the Union of South Africa is not strong, the total number in the Union being 219,928. Three migrations from the Orient to South Africa took place during the last century and a half—Indians, Chinese and Malayas. It is noteworthy that the Indian emigration to South Africa proved far more successful than the Chinese or Malay emigration. Only 2,000 of the Chinese immigrants have now survived; the Malays have intermarried with the Hottentots, but the Indians have transformed themselves from indentured labourers into thriving small farmers and merchants and are now spread all over the country. In South Africa the Indian emigrant saved the sugar estates and the new colony from an impending ruin and developed vegetable gardening to a fine art and wholesale trade and retail-dealing as a lucrative profession in the cities. But discrimination in political franchise, land holding, trading licence and municipal by-laws has for some decades resulted in heaping economic burdens on the Indian in a competition regulated in the interests of the Boer who hardly shows imperial patriotism. In Natal the Indian was deprived of the parliamentary franchise in 1898 and of municipal franchise in 1925. Even the "limited residue" of Indians does not obtain the social benefits to which they are entitled as a permanent section of the population. The "mothers' grant" or the provisions of the Disabled Pensions Bill are not extended to them; while illiteracy is also rampant, about 20,000 Indian children of the school-going age being unable to attend

schools. In Transvaal the Indian was debarred from residence or trade in specified areas in 1932. The allegation of further penetration of Indians into European areas has been proved unreal by the Murray Commission. Yet the segregation of Indians in limited areas where residential land is scarce results in high rents which handicap business and fall particularly heavily on the poorer section of the Indian community. In the Cape Province alone the Indians have the municipal, provincial and parliamentary votes, subject to an education test. The scheme of assisted emigration to India, which was the outcome of the Cape Town Agreement of 1927, and according to which 20,000 Indians were sent back to India, has practically failed due to the conditions of economic life in India and the fact that 80 per cent of the Indian population of the Union are now South-African born. While many avenues of employment are closed to the Indians, there has been a decline in the percentage of Indians employed in industry. The general tendency seems to be to confine the Indians more and more to retail trade. Recently the South African Government have suggested measures calculated to bring about segregation for the Indians occupying their own territory and a scheme of servitude applying to property held by Europeans which will lead to their virtual segregation. Both these have been opposed by the Government of India on the ground that the principle of segregation is not acceptable until the 1927 Agreement has been terminated; but bills on the subject have just been introduced (1939) in the Parliament of South Africa. In Kenya, where the Indians established themselves long before the British appeared on the scene, an order-in-council has been proposed (1939) for the purpose of reserving the Highlands for Europeans. Similarly, in Southern and Northern Rhodesia and Nyassaland, the administration has enunciated its policy of preventing the further entry of Indians who number only about 3,000; while in Tanganyika, where the bulk of the trade is in the hands of about 20,000 Indian settlers, an ordinance for the control of marketing seriously threatens their activity. In Mauritius (281,000 Indians,

comprising 70 per cent of the total population) Indian workers in the sugar plantations and factories earn exceedingly low wages and are subjected to humiliating disabilities. Nor is there much promise of settling Indians in British North Borneo, British New Guinea and British Guiana, as recently suggested by the Colonisation Enquiry Committee. In the unexploited monsoon coast of East Africa the Indian penetrated centuries before the European's advent not only as a trader, money-lender and grain-dealer, but also as a small farmer who introduced the benefits of plough and well irrigation and rotation of crops brought from the mother-land. Economic discrimination against him in the matter of trade licence and land ownership is equally evident in this region.

As in Natal, so in British Guiana, Jamaica and Trinidad, the indentured Indian labourer settled as a free man until the free Indian population far outnumbered the population indentured on the estates or mines. Coolies have been replaced by farmers, fruit-growers, artisans, traders and merchants on a considerable scale, and a sprinkling of professional classes is also found. There are now about 320,000 Indians in Guiana and the West Indies. The Indian settlers in British Guiana (136,000), who constitute 40 per cent of the total population, suffer from the evils of illiteracy and economic serfdom; while in Jamaica (18,000 Indians) Indian marriages according to traditional rites are not recognised by law. Unemployment is now rife both in British Guiana and Jamaica. In the latter island, except for a few storekeepers, scattered here and there, the Indian community is still an agricultural and labouring one, the majority of whom now do not obtain work for more than two days in a week. The Indian population is changing the character of parts of the British West Indies; already a third of the population of Trinidad and 40 per cent of the population of British Guiana are Indians. They have brought here knowledge and technique in rice cultivation, and to their skill is due the first development of the rice industry which has expanded until rice acreage comprises about 30 per cent of the cultivated area

in British Guiana. As a rule the Indians have migrated to countries under the British flag. Apart from small negligible settlements in Indo-China, the Dutch Indies, some Pacific islands like New Caledonia, Reunion, and the Mozambique, the only significant exception is Dutch Guiana, with its 57,000 immigrants from India, which represents an overflow from the adjoining territory of British Guiana and the United States with nearly 5,000 Indian immigrants.

Indian, Chinese and Japanese movements.—The Chinese and Japanese, on the other hand, show no special preference, and have migrated to new lands in need of the pioneer's toil without regard to any political consideration. In the Pacific the Indians have established an outpost in Fiji, as the Japanese have done in Hawaii and the Chinese in Samoa, the Society Islands and the Marquesas. In Malay the Indians preceded the Chinese by nearly ten centuries, but to-day the Chinese outnumber the Indians by four to one and hold the stronger position here, the latter being confined to unskilled and less remunerative lines of work. Similarly in Dutch East Indies, in spite of the civilising influence of Hindu colonisation in Java, Sumatra and Bali in the centuries past, the Indian settlers are far out-numbered by the Chinese, who are now reckoned at about 1,234,000.[1]

Generally Oriental migration, like all mass migration, has been geographically limited by latitude and isotherms. Yet it appears that the Chinese, and in a less measure the Japanese, exhibit a wider range of colonisation than the Indians. This is perhaps due to a greater adaptability of the yellow races to climatic variation. This is certainly a disadvantage for the Indians, who are strictly confined to the zone of 20° N. and 20° S., which is that of the mean latitude of India. For this implies that Indian emigration will be confined chiefly to the tropical regions, and its future is bound up with the intricate problems of tropical hygiene and sanitation.

[1] For details compare the writer's "Indian and Chinese Labour in Agriculture of South-East Asia," *The Modern Review*, Calcutta, December, 1933.

Mass migrations.—In the three Oriental countries with developed civilisations, India, China and Japan, the human reservoir is full to the brim and is now running over. Among these China has shown a more active migration pressure since the Chinese Revolution and its aftermath of internal disturbances. No doubt, all things being equal, geography and ecology will govern the limits of colonisation and settlement of the diverse Oriental peoples.[1] Political and economic opportunities being equalised, the migrants will be more successful in regions whose climate and botanical resources are similar to those of their own homelands. Thus the Chinese and the Japanese expand into and struggle for supremacy in North Manchuria, Mongolia and Siberia where they meet also an attenuated stream of Russians. A similar meeting ground of Oriental migrants, Chinese and Indians in this case, is Indo-China and Burma, into which streams of settlers from the over-saturated Provinces of India and Southern China are now pouring. The frontier between China and Burma has little ethnic or cultural significance. The Shans of Western Yunnan resemble closely the peoples of the Shan States of North Burma, both being represented by the great "Tai" stock which has been gradually displaced southwards. "It is noteworthy," observes Roxby, "that in this far south-western borderland in contrast to the region farther north, the Chinese are rapidly colonising the uplands but are leaving the valleys below 4,000 feet to the Dhans, who are better acclimatised to tropical conditions." In British Malaya the Indians ought to have succeeded better than the Chinese from the southern Provinces of China, which also distributed themselves in the decades past in the neighbouring territories of Annam and Tonkin and are now penetrating into Siam. The Indian farmer is also attracted by the tropical forest regions of Northern Australia, Central and South and East Africa and Brazil. But in all these regions, excepting Tanganyika territory, where there cannot be any discrim-

[1] For the criteria of successful colonisation of Orientals, see the writer's "Population Pressure and the Migration Problem in Asia" in the *Indian Journal of Economics*, July and October, 1933.

ination against aliens, the Indians have met with resistance or discouragement.

In Brazil, which has been the chief destination of the Japanese overseas migrants since 1924, Indian emigration was also encouraged for the exploitation of vast agricultural and industrial resources. As a result of economic depression and unemployment, a restrictive decree was, however, passed in 1931. More congenial for the Indians are the hot monsoon regions in the West Indies where they have contributed materially to population growth, agricultural prosperity and civilisation.

As congenial but perhaps more important in the future for the migrant Indians are the undeveloped monsoon lands, as the East African and North-west Australian coastal plains, where the Indian agricultural experience would be as invaluable as that derived in North China and Manchuria would be for the uncolonised steppe-lands of Siberia and Canada. The Tamils of South India who have emigrated to the northern plains of Ceylon have introduced an extensive and comparatively efficient cultivation of rice, tobacco and vegetables without the aid of irrigation tanks, and their adaptive cropping, well-irrigation and agricultural methods in the dry zone present a striking contrast with the traditional Sinhalese village cultivations in the wet zones.

Economic reconstruction.—Dudley Stamp has observed: "Indian agriculture, as far as crops are concerned, could be applied to a considerable part of uninhabited Northern Australia. When the time comes for the development of this great area of Northern Australia the lessons learnt in India will be invaluable. It is scarcely too much to hazard that in the dry, light soils of North Australia the oil-seeds, particularly perhaps the groundnut,[1] will prove a salvation as they have done over much of the dry belt of Burma." The introduction of the camel into the Australian desert by the Indian emigrants had already been an important achievement, but the full agricultural benefits of Indian

[1] Perhaps also sesamum, mustard, linseed and Kathiawar cotton.

colonisation could not be reaped. Similarly, the introduction of East Indian cattle to Jamaica has also resulted in revolutionising the working cattle of the tick and lice-ridden tropical island, giving them immunity from disease as well as strength of limb, speed of action and weight they never possessed before. In fact the importation of exotic economic plants and animals evolved in similar climatic regions contributes materially towards agricultural reconstruction.

Given free opportunities of migration, the Indian peasant with his traditional skill and method of rice culture may introduce a new era of prosperity into the Guianas, the lowlands of Brazil, the Central American and West Indian region, the Guinea coasts of Africa and the Zanzibar region, as his dry crops, especially oil-seeds, cotton and dry cereals (such as jowar, bajra and marua) may prove a godsend to such sparsely peopled regions as Sudan and Nigeria, Mozambique, Madagascar, and North Australia. Rice is the largest user of wet lands in the world. In Central and South America there are vast areas of uncultivated or semi-cultivated land which is too wet to permit the profitable cultivation of ordinary rice and such root crops as aroids (*Alocasia, Collocasia, Amerphiphallus* and *taro*) or vegetables like chillies, spinach and postulaca, which have been cultivated in the tropical and subtropical regions for centuries, might be introduced. No people are better than the Indians in speedily reclaiming and colonising swamps and river-bottom lands and making profitable use of them by the culture of rice and various kinds of vegetables and tubers. The success of the Indian peasants, cultivating in knee-deep water in the delta regions of Burma and Guiana amply testifies to this.

The Japanese and Chinese in the cold temperate regions.—Indian emigrants have also gone to British Columbia, but both cold temperate Canada and Siberia are far more suitable as outlets for the surplus population of Japan and North China than for the Indians. The Chinese and the Japanese may with cold and drought-resistent wheat,

millets and seeds successfully push the farm line farther into bleak and arid North America where large areas not well suited to ordinary cattle might also well be given to the pasturage of yaks imported from the high regions of Central Asia. Much of the success of Chinese colonisation in North Manchuria and Siberia is due to the fact that the Chinese cereals-beans, kaoliang, corn, maize and millet succeed much better than the Japanese or Russian cereals in this climatic region.[1] The Japanese semi-tropical rice culture is not at all suitable here, while the Russian cereal crops, wheat, rye, oats and barley, are also not adaptable to climatic conditions. As Manchuria, Inner Mongolia and Siberia have now become fields of modern Chinese colonisation,[2] similarly the Chinese can push effectively the frontiers of cultivation in the arid upland regions of the Canadian West where the North Chinese and Manchurian crop, kaoliang, oil seeds and beans, will be able to resist drought periods of considerable duration. Already the introduction of *proso* (which is a great food staple of Turkestan and Siberia) and of Chinese kaoliang into some of the arid states of America such as Minnesota, Oklahoma and Texas has proved to be the mainstay of the American colonists. Similarly the drought-resisting millets, oil seeds and grams of North-western India could be usefully introduced by Indian peasant colonists into the barren semi-arid stretches of Canada. Thus vast arid areas in North America which are now settled only by cattlemen can be brought under the plough and the harrow if the Chinese and Indian immigration be encouraged on a reasonable scale.

But the policy of Oriental exclusion stands in the way of a fair distribution of the world's unutilised lands which a scientific human ecology envisages. Even next door to China the Mongol People's Republic, under the Soviet Russian influence, has now forbidden the entry of Chinese immigrants into Outer Mongolia. Since 1900 and 1902

[1] Yashnoff, *Chinese Colonisation in North Manchuria.* See also Bowman: *Limits of Land Settlement.*

[2] Roxby, "The Expansion of China," *The Scottish Geographical Magazine,* March, 1930.

the United States extended Chinese exclusion measures to the Hawaiian and Philippine Islands; the Japanese large-scale enterprises are threatened with expropriation in the Philippines, while across the seas Indo-China, whose inhabitants have paid their homage to the Celestial Emperor for centuries, now under the French suzerainty discourages Chinese settlement by preventing the Chinese from acquiring rights in land and subjecting them to heavy taxes. New concessions of the red ground are not made to Chinese settlers in Indo-China, while taxes, it is estimated, are seven times as heavy for a Chinese coolie in Cochin China as for an Annamite. Besides, the Chinese or Indian coolie has to give guarantees when he disembarks, and pay a considerable sum when he is taken on as a labourer.[1] A few years ago the French colonial administration followed a discriminatory policy against the Chinese traders who have practically monopolised the internal trade of the region, as the result of which trade greatly suffered. Recently, the administration has dealt rather harshly with Chettiar bankers from India who have lent vast sums to agriculturists especially in Cochin China and Cambodia. The policy of protection of the peasants in the years of agricultural depression as determined by the Long Term Credit Office at Saigon has involved a drastic reduction of the principal and interest of the agricultural loans and a long postponement of the realisation of dues, which have caused hardship, spread distrust and alarm and have led to a withdrawal of more than half of the Indian capital invested in Indo-China. The discrimination against the foreign national also holds good in French Oceania which has recently passed severe restrictive measures against Oriental immigration. Such discrimination is, however, unknown in Siam which, though still empty, contains more than thrice the number of Chinese found in the neighbouring French colony. Similarly, Dutch East Indies, whose vast resources lie hidden in jungle and morass, have followed a systematic policy of organised free emigration as far as contract

[1] Dennery; *Asia's Teeming Millions*, pp. 133–135.

labourers and free labourers in the big enterprises are concerned, shortening of the contract period, gradual reduction of the penal sanction and an ever improving labour legislation contributing to maintain a steady flow of Chinese and Indian labour towards the rubber and pepper plantations and mines, which are gathering the fruits of liberal measures started half a century ago.[1] It is under the Anglo-Saxon and French auspices that colonies and dependencies have followed exclusive and illiberal policies, making more and more difficult the problems of population adjustment in the Orient.

Future of Asiatic migrations.—Such exclusion or restriction will have far-reaching effects on the course of Oriental migrations in the future. First, there will be a stronger tendency for the Oriental emigrants to crowd together and compete with one another as, for instance, in the undeveloped south-eastern monsoon lands, or in Siberia and Mongolia through the gateway of Manchuria. All these regions are being converted into danger-spots, vestibules of invasion and immigration in the Orient. Secondly, there will be an increasing tendency for the three Oriental non-equatorial peoples to migrate to the equatorial rain forest region in Asia and extend the frontiers of cultivation. Here their severe and endless struggle for existence with other forms of plant and animal life such as work on the land involves would lead to high mortality, debilitation and racial decadence. No race, however hardy or virile, can long withstand the climatic handicaps of either the taiga and tundra of Siberia and Mongolia or the wet jungle of equatorial Asia. All this forebodes a serious peril to the Orientals.[2]

Asiatic Emigration within Asia.—Of the monsoon lands in Eastern Asia, Burma and the Malay Peninsula are still comparatively empty. Indo-China is fast filling up, Annam and Tonkin being already developed and, indeed, crowded.

[1] See Dekat Angelino, *Colonial Policy*, Vol. 2, Ch. VII.
[2] See Mukerjee: "Economic Aspects of Asiatic Emigration", *Proceedings of the International Congress of Population*, Paris, 1937.

The following table would show the mass movement of the Chinese and the Indians from the overcrowded plains of the Ganges and the Yang-tse-kiang and Si-kiang to the peripheral monsoon lands which are relatively under-populated.

Undeveloped monsoon lands	*Total Population*	*Population per sq. mile*	*Number of Chinese settled*	*Number of Indians settled*
Burma . .	13,212,000	57·0	150,000	1,300,000
Malaya Peninsula	4,385,000	81·8	1,800,000[1]	770,000
Siam . .	11,684,000	58·4	1,900,000	100,000
Indo-China .	21,510,000	71·9	700,000[1]	6,000
Philippine Islands	12,251,000	104·0	87,000[1]	Not known
Formosa . .	4,600,000	315·0	4,511,000	Nil

There has been more or less an unbroken and unvarying penetration of Chinese and Indians into these relatively unoccupied lands where, while the natives set up their villages in the fringes of the primeval forests, the immigrants fell trees, lay out plantations, open up mines and found towns. The rate at which the reclamation is proceeding will be evident from the fact that in one single year (1927) as many as 428,343 immigrants (figure for 1927–28) entered Burma, 515,394 entered the Malay Peninsula, 142,522 entered Siam and 63,888 entered Indo-China. The same year saw a movement of 303,167 to Ceylon and 45,566 to the Dutch East Indies. This may be compared with the northern migration into Manchuria where the number of immigrants in the same year (1927) was 1,021,942, which is about 125,000 less than the total annual movement into Burma, Malaya, Siam and Indo-China.

The following table would show the spill of peoples over into the under-populated equatorial jungle region:—

[1] Includes estimates of Chinese immigrant population for 1930 prepared for the Fourth Conference of the Institute of Pacific Relations. 1,575,000 is the figure given for the Chinese in Malaya in *Economic Conditions in British Malaya, 1931*, and 418,000 in Indo-China in *Economic Handbook of the Pacific Area*. The Philippine and Formosa figures of Chinese include Japanese. The Siam figure of Indians includes Burmese, Indians and Karens.

Undeveloped equatorial lands	*Total population*	*Population per sq. mile*	*Number of Chinese settled*	*Number of Indians settled*
Ceylon . .	5,125,000	202	—	1,133,000[1]
Dutch East Indies	60,732,000	82	1,240,000	27,638[2]
British Borneo .	900,000	11	50,000	1,298[2]

On the whole the spill over the north is more than double as heavy as that to the south and south-east.

Number of Asiatic Settlers in Asia and Oceania:—[3]

Regions	(*in thousands*)
Manchuria, Mongolia and Asiatic Russia .	35,500
Undeveloped monsoon lands . . .	11,550
Undeveloped tropics	2,450
Polynesia	145
Melanesia	66
Micronesia	13

The pioneer regions in South-Eastern Asia now contain roughly more than 10 million Chinese and 3 million Indians, and in all about 13½ millions of Oriental emigrants, while in the cold temperature regions in the north have settled about 32½ millions of Chinese, Japanese and Koreans.

Arenas of race conflict in the East.—The expansion of the Asiatics into Oceania has been accompanied by a phenomenal reduction in the number of the native races due to economic pressure, the importation of new diseases and the culture contact involving myriad crises of adjustment. In Indonesia, however, instead of the decline of the indigenous race, there has been both an expansion of Asiatic immigrant and native populations, who are still fast multiplying in close proximity to the relatively uninhabited Australian continent. In the Malay Peninsula, Siam, Sumatra and Borneo where the jungle is yet more important than the

[1] Including half-Indians. Excluding half-Indians, the Indian population is 855,000 according to the last Census, 1931.

[2] Figures given in Indians Abroad Directory, 1933, prepared by the Imperial Indian Citizenship Association.

[3] All the tables in this chapter are derived from the present writer's recent work on *Migrant Asia—A Problem of World Population*, published from Rome by the Comitato Italino per lo Studio dei Problemi della Popolazione.

mining town or the plantation, the contact of races is unaccompanied as yet by racial antagonism. On the other hand, in the Philippines, in Burma, Java, Ceylon and Indo-China, the dominance of the immigrants is fast creating, or has created, a race situation full of social risks; wherever the immigrants have turned more to trade, money-lending or clerical employment than to labour on the land or have competed with the natives as coolies doing menial duties, the chances of social outbreaks have been greater. In all these immigration countries in South-East Asia, the functioning of the foreign Asiatics has aroused popular indignation not because of their competition with Western business—though this in some cases extends to banking and insurance as well as trade in commodities—but because of the obstacles it places in the way of the rise of an indigenous middle class. This has led to restrictive legislation in some form or other in the Philippines, Indo-China and the Netherlands East Indies. Even in Burma, which on account of its proximity to India is the best safety valve for her population pressure, there recently has been evident an anti-Indian feeling both in the ports and in rural districts. A number of factors has promoted it, such as economic competition between Indian and Burmese labour in the ports and dock-yards, inter-marriage between the Indians, settled in Burma, and the Burmese, and the transfer of agricultural lands to Indians due to the failure of Burmese cultivators to pay off their debts during the period of agricultural depression. Riots and disturbances have occurred and tension still continues in some areas. It is likely, however that restrictive immigration laws will be passed before long to control the entry of Indian labour into Burma. Following the riots in Rangoon in 1938 about 11,000 Indians have been repatriated. The Indian population settled in Burma now numbers 1,300,000; while the harvesting of rice has in the past led to a sudden increase of demand of labour which could only be met by the seasonal emigration of labourers from India. Similarly, in Malaya, where there are no legal restrictions upon the status of the Oriental immigrants, there has been conflict with natives

in competition for work, rather serious in the Unfederated Malay States. Ceylon, where the utter collapse of rubber affecting about 100,000 labourers caused unemployment, has also exhibited signs of labour unrest and resentment against the Indian immigrant labourers. The problem of unemployment has since become acuter, and recently the Ceylon Government have proposed to discontinue summarily from government service all daily-paid non-Ceylonese workers (mostly Indians) numbering about 10,000. In Fiji the Indians, who were brought by a system of indenture and have settled themselves as farmers, now hardly expect the renewal of their leases of agricultural lands on fair terms. In each case, as the Chinese or Indians expand into these lands, the natives, such as the Burmans, Malayans, Annamites, Javanese, Sinhalese or the islanders of Oceania, are subject to an inevitable process of economic competition, and feel that they have been deprived of work. The feeling becomes stronger the greater the hardships due to lack of employment in the period of depression and shrinkage of markets.

Impelled by the pressure of population, the Japanese also are strengthening their influence in Manchuria and are now engaged in the forcible conquest of China. Similarly, the peaceful penetration of the Chinese in Cochin China, Cambodia and Java and of the Indians in Burma is accompanied by race friction, which also sows the seeds of future conflict among the Orientals themselves. Sooner or later, however, with the emergence of a common Asiatic feeling of humiliation and resentment against the West at racial discrimination, the forces now pent up in narrow Asiatic surroundings may burst out and reach the outer territories, when the arenas of conflict may be shifted to Australia, New Zealand and the opposite shores of the Pacific and the Indian Oceans.

From imperial to international agreement.—India possesses some special advantages in the solution of her migration problem by being an integral part of the British Commonwealth of Nations, which is predominantly coloured. Ninety per cent of the population of the British Empire is non-white. Accordingly neither racial prejudice nor narrow

nationalism can long thwart a rational policy of migration within the Empire. For the establishment of a stable equilibrium between population and living and economic standards on the one hand and climatic and ecological factors on the other is, like tariff and industrial co-ordination, essentially an imperial problem.[1]

Indeed, the solution of the Indian emigration problem by mutual agreement and on the basis of justice and freedom for all, irrespective of race or colour, is intimately bound up with the solidarity of the British Empire with its far-flung dominions inhabited by dark, brown and yellow races. The attainment of full self-government in India carrying with it the possibility of retaliatory measures will also indirectly safeguard the interests of the Indian settlers overseas. What imperial statesmanship may achieve for a group of nations will show the way for a similar solution of emigration problems in the wider international sphere. Great Britain has hitherto taken a prominent part in endeavours to secure world peace and promote the success of the League of Nations and other international organisations. The British Empire to-day comprises the greater part of the unoccupied or inadequately developed sections of the earth needed by its crowded peoples. It is inevitable, therefore, that Great Britain and the self-governing dominions will lead an international movement for a fairer distribution of the world's labour and resources, the lack of which now threatens world peace. Bilateral, multilateral or international agreements based on universally accepted principles of social welfare ought now to replace unilateral action which favours a much more vigorous policy of rejection than has ever been practised in the past and is embittering race relations in the East as well as the West. If all the nations co-operate in formulating an international migratory code laying down universally compulsory standards,[2] Oriental labour instead of being a

[1] See the writer's "Trend of Asiatic Migration" and "Asiatic Emigration in the light of World Economy" in the *Calcutta Review*, November, 1933, and January, 1934.

[2] For the elements of such a code, see the writer's "Inter-National Aspects of Emigration," in *The Indian Review*, October, 1933; also *Migrant Asia: a Problem in World Population.*

menace to the standard of living of the country of immigration will inaugurate a new era of production, while vast areas which are now empty and barren or where agriculture is at a low ebb will be brought in line with the trend of the world's economic progress. On the one hand, colonisation should not be left in the hands of emigration agents, land magnates and exploiting groups but be systematically controlled by the Governments concerned. On the other hand, between several Governments and countries there should be a mutual agreement formulated, if possible, into an international migratory code so that the possibilities of friction due to racial discrimination in the policy of immigration and undesirable racial contact may be minimised. We have the international machinery that could, boldly used, dispense with the barriers, economic and political, and introducing appropriate human material into vast voids or undeveloped regions provide elbow room for all, increase the world's food supply and production and level up the standards of living among the nations.

APPENDIX

CHINESE

Country	*Number*	*Percentage of total*
Siam	1,900,000	19·0
Indo-China	700,000	7·0
Malaya	1,800,000	18·0
Borneo	150,000	1·5
The Philippines	70,000	0·7
British North Borneo	50,000	0·5
Hawaii	25,310	0·2
Dutch East Indies	1,240,000	12·4
The Pacific Islands	50,000	0·5
Australia	20,000	0·2
United States	74,954	0·7
Canada	45,000	0·4
Other countries	3,874,736	28·9
	10,000,000	100·0

INDIANS

Country	*Number*	*Percentage of total*
Burma	1,300,000	31·6
Ceylon	1,133,000	27·5
Malaya	628,000	15·2
Dutch East Indies	27,638	0·67
British Guiana	130,075	3·2
Trinidad	133,277	3·2
Dutch Guiana	57,600	1·4
Fiji	76,722	1·9
Mauritius	281,000	6·8
Kenya, Tanganyika and E. Africa	86,220	2·09
South Africa	186,000	4·5
United States	4,901	0·1
Australia	2,000	0·05
Canada	1,200	0·03
Other countries	77,367	1·8
	4,125,000	100·0

JAPANESE

Country	*Number*	*Percentage of total*
Manchuria	243,260	12·8
China	55,708	2·9
Hawaii	134,042	7·0
Philippine Islands	16,667	0·8
Mandated Islands	17,800	0·9
Continental U.S.A.	140,945	7·4
Canada	22,664	1·2
Brazil	103,166	5·4
Formosa	220,270	11·5
Malaya and Borneo	19,652	1·0
Dutch East Indies	5,000	0·2
Korea	530,000	27·8
Saghalien	284,345	14·9
Other countries	116,481	6·1
	1,910,000	100·0

CHAPTER XXV

ECONOMIC PLANNING

By The Honourable Mr. Nalini Ranjan Sarkar
Finance Minister, Government of Bengal

Planned Economy has passed from the sphere of theories into the realm of practical politics and is to-day a compelling question for politicians, consequent on the growing volume of public opinion, both expert and lay, in favour of planning. In England there seems to be wide agreement that "leisurely politics will only lead to a sense of frustration and despair. The public is profoundly distressed by the volume of present-day misery. There can be no more dangerous threat to Democracy than complacency at a time when so many millions of our people are burdened with poverty and unemployment, and yet are convinced that society can be more sanely organised." Influential sections of public opinion in England are now inclining towards "a coherently planned reconstruction of the nation's economic life, for readjustment of the social order as well as imaginative development of the land." The same may be said of India with added force, but we yet have to contend here with a school of thought that still seems to believe too strongly in the time-worn doctrine of *laissez faire*.

The demand for planned Economy is the result of waning faith in the mystic qualities of *laissez faire*, and it is incumbent on us all to examine how far economic planning is practically and theoretically defensible. We must admit that the theory of the orthodox economist, *viz.*, that under a free economy economic forces tend towards the equilibrium and that neither depression nor boom can come to stay, and that, on the whole, the cyclical phases of an individualist

economy tend towards progress, is fundamentally sound. But the theoretical exponent of *laissez faire* has been too prone to assume that the conditions of his reasoning can be reproduced and maintained, without serious dislocation, in the practical world. Pure individualism is, undoubtedly, an abstraction. In earlier periods of history the economic organisation answered roughly to the description of a free economy; and the advantages claimed for this system were reaped in large measure by every progressive community. So long as there was a balance of advantage in free competition and the non-interference of the State in economic matters, orthodox principles of economics were accepted by large masses of the public and were challenged only by Utopian extremists. But the last few years, which have been characterised by an unprecedented depression, have clearly disclosed its essentially "deadlock" character and have aroused in some minds the suspicion, and in others the conviction, that the system of free competition as it obtains to-day has no longer the qualities necessary for automatic readjustment within a reasonable period of time.

There is still a large body of academic economists who are concerned to point out the risks of a planned economy and to emphasise the value of *laissez faire* as a self-regulatory economic principle. But the large masses of the public of all classes are definitely averse to the sluggish working of the doctrine, which, not unoften, entails in the process considerable misery to the people. They see that the principle of *laissez faire*, although it may appear to be the best in pure theory, does not work out satisfactorily in practice and that the various forces at work in our economic activities lead to the emergence of vast monopolies and other various restrictions which are inimical to the interests of a *laissez faire* economy. They are, therefore, led to believe that the system of free competition cannot be preserved indefinitely without the necessity of State intervention of some kind.

From the practical standpoint, the supporters of *laissez faire* to-day are on even less firm ground. Public opinion presses increasingly for economic improvement, for economic

and social justice and its representatives are compelled to demand measures to satisfy the public desire. It forces them to scrutinise the repercussions of direct and indirect expenditure and even in the most individualistic countries, gives rise to many demands that require to be adjusted and reconsidered. Even in the nineteenth century the institution of measures of social reform such as graduated taxation of income and property, old-age pensions, unemployment insurance, labour exchanges, etc., seemed just and expedient to all but a few. These measures of social relief were widely accepted and it is futile for *laissez faire* economists to resist their extension on the grounds of aggravating the maladjustments and increasing the rigidity of the economic system.

The important fact to-day is that while social changes do not interfere too greatly with the even tenor of the economic life in the prosperous years, during the depression they have come to weigh heavily on the national finances and form one of a number of obstacles to the readjustment of cost and price, without which a recovery from a depression is impossible. But the elimination of any measures of social relief is unthinkable; the public demand their extension; we cannot afford to ignore it and must accept it as a fact to-day.

Similarly, protectionism has to-day to be accepted as a fact to be reckoned with. Protection is the only means of affording to the undeveloped nations of the world a reasonable scope for national economic development. Even orthodox *laissez faire* economists have always admitted that protection to an infant industry is sometimes an indispensable necessity. In many countries protection, as exemplified in the exaggerated regard for national self-sufficiency, has been accorded the status of an official religion. It may, indeed, seem to many, at first sight, that protectionism, as it obtains to-day, is only one of the follies of a capricious nationalism. Such a view needs, however, to be weighed against the fact that so far as the industrial nations are concerned, the protected industries arose in the exceptional circumstances which ruled during and immediately

after the war, and once vested interests arise round a new business, Government has to think long before reducing the protection, without which the industry might be ruined. Thus, for various reasons, many apparently uneconomic enterprises have been allowed a long lease of life. It should not, however, be forgotten, even in respect of such instances, that their uneconomic character has often been diminished by the progress of science and industrial technique. Some time ago Mr. Keynes pointed out in a frank exposition of "Economic Self-sufficiency" that the theory of international free trade has been nearly battered by the fact that the progress of science has enabled every country to produce a far wider range of goods and services than in the past and that, therefore, the geographical division of labour, on which the theory of international trade was based, is no longer true to the same extent. In other words, the progress of science has encouraged the belief that the protected industries are likely to become economic propositions. When to this belief is added the fear that post-war pacifism has evaporated and that the next war might be on the world at any time, the reluctance of Governments to abandon the new industries to their fate can be easily understood. It is, therefore, useless to hope that the protectionist barriers to international trade will be swept away.

The persistent progress of protectionism has made it nearly impossible for the world to return to a régime of free international trade. For the duplication of productive activity which results from protection and the entry of new nations like Japan in the world markets have intensified competition and necessitated the adoption of protection even in countries like Britain to whom free trade had been the breath of being. The intensification of competition has also led to such abuses as dumping, which in turn aggravated the protectionist sentiment in the country victimised. Again, the currency and exchange system is tampered with and the world has seen a complete disorganisation of the system of international finance which obtained in the days of free trade. However much one may believe in free trade as

the panacea, one cannot but admit that the wide path to free trade has at present been narrowed by innumerable obstacles. With the best will in the world, the Governments would find it nearly impossible to restore either free trade abroad or *laissez faire* at home, and equally is it impossible, as has been pointed out already, that free competition can continue indefinitely in a capitalistic economy. The truth of this statement was brought home to everyone by the depression. For this reason, there is a universal demand for the regulation of economic life on the basis of a thoughtful plan.

The demand for Planned Economy is thus best understood as a demand for economic life to be preserved from the capricious mercies of blind economic forces, and for a fair assurance of an even tenor of economic life in the country. This demand is both just and natural. Socialists and Communists are apt to assume that a demand for Planned Economy signifies an abject surrender to their claims on the part of those sections of the people who were formerly opposed to their cult. Individuals, too, often commit the error of admitting that the advent of economic planning means the death-knell of all private enterprise and the triumph of Socialism. But from what I have said above, it should be clear that the demand arises only from a disillusionment as to the self-regulatory character of a free economy and a recognition of the particularly tangled nature of national and international economic life. Though planning necessarily means a far greater degree of State initiative, it does not mean a rigid delimitation of the scope for private enterprise. The value of a planned economy lies in the provision of safeguards against miscalculations and maladjustments, the fluctuations of booms and depressions. It also means the frank acceptance by the State of full responsibility for the protection of economic life. There is nothing in either of these which would necessarily lead to the economic regimentation associated with State Socialism. For my part, I believe that planning affords a broad common ground of action, from which various schools of economic thought have so far been kept off by

the acceptance of diametrically opposite principles, thus never being able to come to grips with the crucial problem.

Objective of Planning

What should be the objective of a national plan? While the masses would rebel against the thought of bending the energies of a whole nation to the private profit of a few investors, Socialists would find themselves equally out of touch with the feelings of the masses if they endeavoured to make planning a thin camouflage for Communism. The needs which a planned economy should serve will depend largely on the state of the economic development of the country concerned. Given a measure of good sense and good-will, the classes and masses would find it easy to agree on a tentative programme which might well give them the best of both worlds.

The plan would necessarily vary from country to country. A study of the plans which are now pursued by the various organisations of the world will show that an acceptance of one common form or cult is by no means a condition precedent to planning. Soviet Russia which has set the example of planning is a frankly Communist society and pursues a plan calculated to achieve all the ends of Communism. For the fascist nations like Italy and Germany, a planned economy is part of a larger political idealism. The denial of the old kind of freedom of business organisation is derived from the political principles of Fascism. Economically the Fascist State aims at a corporate life which will eliminate all the discords of free competition and ensure that all classes prove their worth in realising the nation's economic potentialities. In the United States the problem is one of ensuring a fair balance between supply and demand, production and consumption. Mr. Roosevelt has interpreted his task as one of creating adequate purchasing power in the hands of the masses, and his economic policy is directed to this end. Great Britain has her task cut out in the shape of adjusting her economic life which she cast in the days of free international trade and industrial supremacy, to a

radically altered world economy. She has to reduce the measure of her dependence on the external world, correct her bias in favour of foreign investment, open up new avenues within the country and effect as happy a compromise as possible between economic self-sufficiency and absolute free trade. This compromise she seeks through a series of trade pacts as an insurance against the decline of her exports and diminishing world trade. Thus, every one of these countries pursues a plan in keeping with its own needs and character as visualised by the party in power, but the main principle is the extension of the State's responsibility in the sphere of economic activity.

India's Case for an Economic Plan

In such circumstances what would India do? There is no reason to assume without enquiry that she must follow the foreign example and plan. The need for planning in India, however, is *prima facie* suggested by certain anomalies in the existing order of our economic life. India possesses outstanding natural advantages in respect of all the aspects of national economy, agriculture, industry and commerce. Yet she remains to-day largely an undeveloped country with an extremely low standard of living. And despite her natural resources and a large internal market, she remains perilously dependent on other countries for the supply of many essential requirements. It seems almost like a paradox that while India is considered by the economic experts of the League of Nations to be one of the eight principal industrial countries of the world, she continues to be mainly an exporter of raw materials and importer of manufactured goods. One of the greatest producers of raw cotton, India imports immense quantities of piece-goods; and though herself the world's largest grower of oil-seeds she looks to other countries for her supplies of paints, varnishes and soaps. With vast acres suitable for tobacco growing, India imports large quantities of foreign cigarettes. In spite of immense resources of bamboo, timber and grass, India imports most of her paper requirements. The same anomaly

is to be observed in India's consumption of foreign leather and leather goods, rubber goods and machinery. As a matter of fact, most of the agricultural commodities which India exports at the present moment may be profitably utilised within the country, if only efforts are directed to the development of the appropriate industries, and none will deny the great need for industrial development in India to offset her extreme dependence on agriculture.

While these anomalies point to the need for formulating a comprehensive plan for consolidating the economic structure of the country, the urgency of planned action will be all the more vividly realised from an analysis of the nature of the problems that now confront us in the varied aspects of India's economic life. Taking the case of agriculture, first, we find that while it provides the mainstay for the bulk of the population in India, it is conducted on an extremely uneconomic basis. It is a matter of common knowledge that the agriculturists in India are overburdened with debt amounting to about Rs. 900 crores, while, as a rule, their holdings of land are extremely uneconomic and incapable of providing them with any surplus to meet their debts. The problem arising from these circumstances demands not only an augmentation of the yield and income from the land, but impinges on the larger question of occupational redistribution of the people. No improvement in the technique of production, however welcome it may be, will alone constitute a solution of the problem of our agricultural economy unless some effective means is devised to reduce the existing pressure on land and divert the surplus agricultural population to other channels. Simultaneously the problem of subdivision and fragmentation of holdings which now offers obstacles to measures of agricultural improvement will have to be tackled effectively. It is also necessary at the same time to deal with problems connected with the improvement of technique, increase in the yields of particular crops, regulation of such crops as are confronted with the danger of over-production, selection of better and more remunerative crops, provision of better marketing and financial facilities, etc. These problems

which are of a secondary character are nevertheless vital. They impinge on the larger problems and no one who has had occasion to examine them will agree that they admit of separate treatment. These reforms can come only as part of a larger plan framed with due regard to other aspects of the national economy.

The growth of industries also in India has hitherto been mainly of a sporadic character. This explains why our industrial progress has lagged far behind, in spite of the fact that India possesses vast resources and a large internal market. Even the development of such industries as have been established gives indication of inherent weakness in the over-multiplication of units in particular lines, and little progress in other equally important lines. In a country like India where industrial investment is by no means great, haphazard growth of this description is deplorable. We require a harmonious development of industries on a diversified basis and particular importance should be attached to those industries which are likely to strengthen our agriculture by drawing out, as much as possible, the surplus population dependent on land. The development of industries on such lines necessarily involves the question of localisation to ensure the necessary benefit to the agriculturists. Localisation will again involve such questions as the availability of cheap power, raw materials, and cheap facilities for communication. The task obviously calls for planned action, with a view to industrial expansion along defined lines, for which the requisite banking and financial facilities will have to be ensured.

Similarly in the organisation of our trade and finance, we need to proceed on a well-planned basis. Planned action is particularly necessary in respect of our foreign trade, for, in the existing conditions of world trade, India's favourable trade balance which is essential in order to allow her to meet the heavy annual foreign obligations, is steadily diminishing. Unfortunately, the commercial policy of the Government of India has not always been guided by this consideration. Though, of late, India has initiated a policy of establishing closer commercial relations with other

countries by entering into trade agreements with certain nations, it cannot be said that all of them fully answer to the requirements of India. The Ottawa Trade Agreement, for instance, does not provide an adequate *quid pro quo* in as much as it fails to ensure to India a favourable trade balance with the United Kingdom to whom she owes the major portion of her foreign obligations. In the circumstances, now more complicated than ever by such world factors as the depression and the growth of economic nationalism leading to the accumulation of trade barriers, it is incumbent on India to follow a well conceived policy in extending the frontiers of our foreign trade, thereby ensuring a favourable trade balance.

The same necessity for a systematic policy appears in the case of internal trade as well. As yet, the Government do not seem to have a definite internal trade policy, with the result that even in recent years we have witnessed in India the curious phenomenon of certain articles being imported in some provinces of India, while the same varieties of articles were being exported from others. While, on the one hand, anomalous and in certain cases discriminating transport charges stand in the way of wider distribution of goods between the different parts of the country, lack of adequate commercial banking facilities, on the other, is impeding the development of internal trade. In a vast country like India, internal trade should be regarded as of vital importance; it actually constitutes over fifteen times the volume of the foreign trade. Systematic efforts are obviously called for to strengthen and develop this aspect of India's economy.

Closely allied to the question of internal trade is the problem of transport. The transport organisation at present shows not only a distinct lack of co-ordination with the economic requirements of the country but also a lack of co-ordination within itself. While in certain areas we have been witnessing uneconomic competition between the different kinds of transport agencies, entailing enormous waste, there are extensive regions in which adequate transport facilities have not yet been developed. The absence

of co-ordination appears in the most acute form between railways linking the ports and the coastal shipping services and also in some areas between road and rail. In respect of the different railways again, we require thorough overhauling of the freight schedules. These schedules were devised to serve the purposes of the export and import trade of the country and do not, therefore, suit the present requirements of the country in view of the development of a large number of indigenous industries. Again, the inland water transport system in India demands special consideration and efforts for development in view of the fact that, as the cheapest means of transport, it suits a poor country like India admirably.

In the sphere of banking, currency and exchange, the necessity of a plan is irresistibly impressed upon us. India's banking system lacks homogeneity and cohesion, apart from the fact that it is not sufficiently developed as yet to meet adequately the requirements of India's agriculture, industry and trade. The organisation of agricultural credit, commercial expansion and industrial progress can be effectively assisted only by the evolution of a well ordered banking system in the country. We do not possess an adequate number of land mortgage banks to render relief to the debt-ridden agriculturists, nor have we developed the necessary banking institutions to provide commercial and industrial finance in a scale and manner required by the economic conditions of the country. These are defects in our economy which require to be removed; and unless progress in banking facilities is made in all these spheres, no well ordered economic development of the country will be possible. Active assistance of the Government is vital at every stage of banking development, which obviously points to the need for a systematic banking policy on the part of the Government. The question of regulating currency and exchange has also an important bearing on many aspects of India's economy. Either in the matter of trade expansion at home or abroad, or in the matter of regulating the internal price levels, particularly of agricultural commodities, a well conceived currency policy favourable to Indian interests

is a prime necessity, and nothing can be more dangerous to the economic interests of a country than a policy of drift in this important respect.

In the matter of the administration of Indian public finance, again, the same lack of plan is manifest. The sources of revenue have changed from decade to decade in point of importance and yield, but the Government of India have not yet succeeded in evolving a satisfactory system of public finance adequate to the growing requirements of India. We still depend for the stability of our public finance upon very limited sources of revenue and the expansion of Government's activities on developmental lines is seriously hampered by the non-expansiveness of these resources. The system of taxation itself is full of defects and inequity.

Unintelligent Government Policy

These are the patent defects of the economic organisation in India, but at the same time it is only fair to point out that the Government of India have not been altogether indifferent to the economic development of the country. Their policy has to some extent swerved from the classical theory of *laissez faire*, for they have from time to time taken measures for the improvement of our agriculture, trade and industry. The institution of the Imperial Council of Agricultural Research and the various Crop Committees, the appointment of Trade Commissioners abroad and the recent trade agreements with certain countries, the initiation of the system of "discriminating protection" for Indian industries, the recent institution of a scheme for industrial research and the enactment of a number of labour laws—these are some of the measures which the Government have undertaken to promote the economic welfare of the country, but these measures lack co-ordination and have not been guided by a consistent comprehensive policy.

The Government of India have thus far pursued an economic policy which falls short of the real needs of

the country. The meagre results of this policy and the anomalies of the system already referred to, serve only to establish the *prima facie* case for planning in India. I have no doubt, however, that if we shirk the obligation to formulate a comprehensive plan and trust the economic destinies of the country to such policies as the Government may have so far formulated, the results will be truly depressing; but the need for planning is not suggested merely by impatience at the present rate of progress. For my part, I contend that the pursuit of the present policies may not only fail to achieve any progress but may even result in a setback. It is well known that, as a result of the depression, the economic life of every nation has become so complicated that the pursuit of any policy that has regard to only one and not all aspects of the national economy is of no avail. In India, particularly, such a policy cannot be followed without the risk of grave repercussions in other spheres. For instance, the policy of discriminating protection was formulated by the Fiscal Commission in recognition of the vast industrial potentialities of the country which lay undeveloped. It is true that the Government have been more or less half-hearted in the execution of this policy, but such effect as the Government have given to its recommendations shows clearly that discriminating protection by itself cannot be relied upon to bring about a harmonious economic development. During the last few years it has become clear that the exuberance of nationalist sentiment has not helped a correct appraisement of the reactions of protectionism in India. The industrialisation which has come about as a result of the protection has not been, as it is becoming clearer, evenly distributed. Our economic problems are rendered unduly complicated if the benefits of protection are not evenly distributed between industry and agriculture or one is helped to thrive at the expense of the other. As the experience of discriminating protection during the decade in which it has been in force indicates, the advantage has gone mainly to the industrial Provinces, with the result that the agricultural Provinces are now inclined to protest against this policy and any Government

in India would in future find it difficult to strike a happy balance. On the one hand, it cannot alienate the sympathies of the agricultural Provinces, and on the other hand it cannot throw open the internal market to the influx of foreign imports. The want of a co-ordinated plan gives rise to many such difficulties.

The policy of discriminating protection also suffers from the failure to consider adequately the relation between Indian industry and Indian agriculture. When it was first enunciated, it was believed that the hardships entailed by protection would be neither considerable nor prolonged and that the infant industries would grow to maturity and easily fit into the framework of both the national as well as the international economy. As a result of the depression and of certain developments in the outside world, the Indian agriculturist has not only failed to receive any compensation for the increased price he has to pay for the protected articles, but he has also been progressively losing ground in the foreign markets. The distress of the agriculturists, as has been hinted already, now threatens to work in the direction of a premature abandonment of discriminating protection.

Another serious repercussion of this protectionism is that the Government of India have been deprived of a substantial portion of their customs revenue. The continuance of this policy would entail a more or less thorough overhauling of our system of public finance. The successive committees which have enquired into the question of Federal and Provincial finances have uniformly failed to evolve a plan acceptable to all parties. It is obvious that a national financial system should be shaped according to the requirements of national economy of the time in which the system will have to function, and the risks are great of a financial plan that has not been clearly thought out in relation to the economic development of the country. It would tend to circumscribe Government's capacity to render help to the country's industry, agriculture or trade.

What, then, will be the nature of the plan which India would be well advised to adopt? Admittedly in the case of

India the plan will have very little in common with those which have been pursued in countries like America or Great Britain or Germany or Italy. India is a country of undeveloped potentialities; and her prime need, therefore, is to develop the resources which have so far remained untouched. In this respect her position bears a closer analogy to that of Russia.

Nature of Planning in India

India's plan will thus be primarily developmental in character, aiming at the development of the existing and potential resources of the country in the most effective manner possible, by co-ordinating and directing the productive processes of the country. This would be the particular distinguishing feature in a plan for India as compared with the plans evolved by the advanced countries of the West. Whereas the chief objective of the plans of these countries is to curtail and regulate production, to put, as it were, a brake on their productive machinery—the essential aim of our plan would be development and expansion, though at the same time we may to some extent have to regulate and rationalise the ill-conceived growth of some of our industries and regulate the production of certain crops. But the latter is certainly not our main problem. Our main problem is to take adequate advantage of the vast potential resources and the large internal market; in a word, to expand our trade, industry and commerce to the fullest extent. Awakened very late to the urgent necessity of industrial development and faced with keen competition from the industries of the Western countries, as well as of Japan, we cannot afford, particularly at this juncture of world crisis, to fritter away our resources by haphazard development.

The reconstructional aspect of India's planning again brings similar problems to those that have confronted Western countries in consequence of the reactions of the slump. In India, also, the depression has wrought many maladjustments in the various spheres of her economic

life and systematic efforts are needed to restore equilibrium and create conditions favourable to the revival of trade, commerce and industry.

Thus apart from the developmental aspect of planning a suitable economic programme for India should also embody measures of a defensive nature, as against the reactions of the economic policies of other countries. India is so vitally interested in the economic developments of the rest of the world that she cannot remain unaffected by their reactions. The rapid changes that are manifest in the economic outlook and policies of other countries, the growth of exaggerated economic nationalism, the economic consequences of tariff barriers and diverse currency policies have been exerting a tremendous pressure upon our economy. To counteract their unfavourable reactions and to diminish the violence of their impact, it is necessary to plan defensive measures for our own protection.

Apart from these economic aspects, there are also social and cultural aspects of economic planning in India. A primary aim of planning is to increase production, not as an end in itself, but for the purpose of guaranteeing better living conditions; and also to ensure economic and social justice as between the classes and masses. As such the social and cultural aspects of Indian life would also require some readjustment. In particular, the excessive growth of population in India should receive our most anxious consideration. The various aspects of the population problem of India can only be widely made known by the spread of education. It is particularly necessary that this education should be available to the masses so that they may fully appreciate the bearings of the population problem on their economic conditions.

The Scope for Planning in India

The scope for planning in India is very large, though not without certain obvious limitations. There are, for instance, the constitutional, or what may otherwise be called external, limitations: there are also "internal" limitations arising

from the social traditions of the country. The Indian social system is innately conservative and it should be realised that any plan likely to create conditions prejudicial to the continuance of the existing social and economic classes will be strenuously resisted.

Again there are the limitations arising from the absence of adequate knowledge and technique, but they will be overcome as we proceed with the plan. The economic data which we possess are inadequate and defective in many respects, and require to be made more comprehensive and up-to-date. The need for authentic data cannot be too much emphasised inasmuch as "the first requirement of a planned economy is a co-ordination of information which reveals the inter-play between economic forces, and economic data that may be depended upon as a rule." The scheme[1] suggested by Dr. Bowley and Mr. Robertson for an economic census of India with special reference to a census of production and reorganisation of statistics does not go far enough, but it may well serve as the basis for a systematic compilation, to be extended and supplemented in course of time.

While drawing attention to these limitations to the scope of planned action in India, it is interesting to note that in one respect the circumstances in this country are particularly favourable for economic planning. In the developed countries, as in Europe, foreign trade has flowed along certain channels for long periods and the features of the economic system are too rigidly set to be easily altered; vested interests offer strong opposition to innovation. In India, however, such problems, even where they exist, are milder and will not prove so great an obstacle. As has been aptly said: "Economic experiments are being made everywhere, but relatively old established communities, with

[1] Dr. Bowley and Mr. Robertson suggested the following tentative scheme:—

1934. Appointment of Director of Statistics.
1935. Organisation of the enquiries and training of investigators.
1935–36. Rural Survey.
1936. Census of production. Urban Surveys. Population and occupation census.
1937. General Report.

their huge accumulations of capital goods and vested interests are often difficult laboratories for work on a nation-wide scale." India is comparatively free from this handicap, and planning may be attempted in India under much better auspices than in many of the other advanced countries.

Methods and Machinery of Planning

In the formulation and execution of a plan for India, we shall have to rely on the combined efforts of the State and private enterprise. While it is true that the execution of a plan entails considerable Governmental control of economic activities, it should at the same time be recognised that much can be achieved in the way of rational development of our trade, industry and agriculture by organised private action which, however, will require to be assisted in all possible ways by the Government, both directly and indirectly. Indeed, certain parts of the plan are perhaps best left to private enterprise.

But the planning as such will, in either case, have to be entrusted to a competent authority. As already pointed out, no plan can be formulated, far less carried into action, unless there is effective machinery set up for the purpose. It is well-known that the existing Governmental machinery is by its nature unfitted to undertake such a task. Yet the planning authority which is to be evolved for India must emanate from and be in close conformity with the existing constitutional structure and this consideration renders the task of organising an appropriate planning body in India not only difficult but also complicated.

Suggestions, however, as to how the requisite machinery for planning may be evolved in India are not wanting[1] and the material at hand may be utilised with profit. The central idea is to set up a supreme Economic Council or a National Planning Commission, which will not supersede either the executive or legislative limits of the Government. It should be composed of a permanent personnel of experts

[1] A scheme for an Economic Advisory Organisation in India, as suggested by Sir A. Salter.

with the right to co-opt from time to time members having expert and specialised knowledge in particular problems when the Council has to deal with such problems. Such an expert body will have a sufficiently wide purview to assemble all the relevant facts, while its permanency is likely to ensure that the plan will gradually and consistently develop in a healthy continuity. The procedure would ensure availability of specialised knowledge of particular problems and at the same time it would guard against too circumscribed an outlook. It would also prevent the Council from growing unwieldy. In the task of planning, each particular industry, manufacturing, agricultural or extractive, should be dealt with as a whole, and the several branches of industry organised for co-operative work. Organisations should be set up for industry, agriculture, retail trade, foreign trade, banking, etc., which should be able not only to represent, as organised functional bodies, their cases to the Council, but also to carry out such schemes as may be entrusted to them. Where such organisations for the whole of any particular economic aspect of life or for the separate branches of any industry do not exist, the setting up of such associations should be actively encouraged.

In respect of the Provinces, too, we should have similar Economic Councils, although, in so far as the services of experts are needed it should be open to these Councils to draw on the experience of the Central Council in addition to their having the right to co-opt members with special knowledge particularly of Provincial matters. An important function which the Provincial Councils will serve is the compilation of relevant data in regard to the various aspects of the economic life of the respective Provinces. Towards this end, voluntary co-operation of universities and colleges, on the one hand, and of Chambers of Commerce, on the other, would be found extremely helpful. Here it may be remarked that while to-day it is recognised that there is a dearth of statistics and other information, the planning Councils would require to be in possession of all relevant facts and statistics in order to assess the economic situation and evolve their schemes on the basis of facts. It would,

therefore, entail their undertaking a thorough overhauling of existing statistics and methods.

The administrative divisions of India, as they are under the existing constitution, suggest also the necessity of co-ordination between the Central Planning Commission and the Provincial Councils. The Provinces are and will be in charge of most of the developmental services, with the result that the responsibility and necessity of planning will devolve mainly upon the Provincial executives. Under the new system of autonomy there will be large scope for the popular executives to plan their policies, though subject to certain limitations, and in accordance with the wide plan adopted for the country as a whole. It becomes, therefore, evident that India will need not one single homogeneous plan but a number of plans and their application will be on a Provincial basis, while the Central Planning Council will co-ordinate and actively assist and supplement their efforts, thus helping the formulation of a unified national economic policy for India as a whole. Such assistance will be necessary to ensure success to any plan or plans that may be adopted by the Provinces in promoting the development of any branch of agriculture, industry or trade, because the Central Government will control the larger policies of vital interest such as those relating to currency, tariff, railways, etc.

It will necessarily fall within the scope of the Central Council to see that a closer inter-provincial co-operation towards a policy of balanced industrial development in the country is ensured. It must be admitted that there is a tendency for certain industries to develop beyond the consuming capacity of their effective economic markets, whereas it should be the aim to afford to each Province the fullest opportunity to develop its own industries, avoiding the dangers of duplication and over-production and the danger of inter-provincial jealousy. In the event of conflicts between the Central Council and any Provincial Council, again, the decision should lie with the Central Government or in whomsoever the residuary functions are vested.

The planning bodies would naturally have regard to the statistics and information obtainable. They would require to be at once realistic in their approach, paying due regard to actual conditions, and sufficiently imaginative to view the problem as a whole in relation to the several parts and with reference to future possibilities. The machinery must be prompt in action, and at the same time flexible. It must be kept free of the bureaucratic influence, courageous to act and courageous to admit mistakes, not hesitating to effect changes in method or policy in keeping with the changing conditions.

As matters stand, it would not be possible to launch a full-fledged economic plan in India in all its details at the very commencement, as in Russia and America, but our procedure should be of the nature of unit planning. There are various ramifications in our economic and social life which have to be approached in an orderly and systematic way, with reference to a unified objective.

Conclusion

In the foregoing pages an attempt has been made to show from the altered conditions of the world to-day, the necessity that faces every country to abandon the theory of *laissez faire* in favour of increasing State responsibility for the economic ordering of the country with equity and humanity. The question always is how far the State's responsibilities should be actively extended and obviously it depends upon the nature and requirements of each State. These circumstances serve to decide the character of the plan to be adopted. A plan implies forethought, co-ordination and purpose, and the existence of suitable machinery to give it effect. It implies useful intervention and regulation, but not needless restrictions. It is conscious direction as opposed to haphazard methods and mere improvisation. So far as India is concerned, I have endeavoured to suggest in barest outline a plan that the circumstances would appear to warrant, and the conclusion to which circumstances readily point is that India would be

well advised to devise a comprehensive plan and proceed to apply it in parts, with a view to initiating a continuous process of co-ordinated planning.

Post-script.—Since these pages were written, certain important changes both political and economic have taken place in India. Although they do not affect the conclusions reached in this article, it is necessary to briefly mention them here in order to indicate that the changes reinforce my views and conclusions in an emphatic way and that the question of economic planning in this country has become a problem of live interest. The inauguration of Provincial Autonomy on the 1st of April, 1937, has ushered in an era of much democratic enthusiasm for social and economic endeavours and most of the Provincial Governments are initiating ameliorative measures in diverse directions. Some of the provinces like Bengal and Bombay and the C.P. have already set up special Industrial Survey Committees in order to investigate into the position of existing industries and to assess their possibilities as also the potentialities of new industries so that they may recommend measures by which a sound and rational process of industrial development may be ensured and accelerated. Besides, the Congress which is in power in eight of the eleven provinces has also set up a National Planning Committee which is now engaged in an enquiry into the existing position of industries and their future possibilities. Thus a stage has been reached at which Government initiative for economic planning is no longer a remote possibility but may be a reality of much practical value, provided a co-ordinated programme of planning is formulated and pursued for the entire country.

But judging from the situation as it is, there seems to be a lurking danger in all these efforts for planning in the fact that the necessary measure of co-ordination between the endeavours of the provinces and those of the Planning Committee may be lacking or may take a very long time to be evolved. Planning to be rational and effective must be viewed on an all-India basis, with at the same time, a

sympathetic and tolerant understanding of the particular needs and claims of the various provinces. It is, therefore, extremely desirable that perfect co-operation should exist not only as between the Provincial Committees but also between the Provincial Committees on the one hand and the National Committee on the other. Collaboration should by no means be limited only among those Provinces where the Congress is in power but should be sought and ensured in respect of other Provinces as well. There is again the question of securing the co-operation of the Government of India in any scheme of economic planning that the Provinces or the National Planning Committee may formulate.

Such collaboration in efforts for economic planning is indeed the essential preliminary to the success of any programme, for in their initial enthusiasm the Provinces may inaugurate measures which may lack co-ordination and may be self-contradictory from the standpoint of the economic progress of the entire country. It is against this danger that utmost precaution is called for.

In the sphere of India's foreign trade, of course, the Ottawa Agreement has been replaced by the Indo-British Trade Agreement and a new pact has been concluded with Japan, but such changes do not very much alter the situation as it was some four years ago. The balance of trade position of India is still today uncertain and provides a genuine cause for concern. No doubt appropriate and planned efforts for expanding India's export trade by negotiating advantageous trade agreements with India's best customers are necessary to meet the situation.



Part V

CURRENCY AND BANKING



CHAPTER XXVI

MONETARY SYSTEM AND POLICY

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I. Currency Evolution, 1835–1925

The silver standard and its fall.—The evolution of the modern monetary system of India may be said to have begun in the year 1835. In the opening decades of the nineteenth century, some parts of the country, *e.g.*, Madras, had a gold standard with gold currency, while other parts of the country, *e.g.*, Bengal, had a silver standard with silver coins and gold coins in concurrent circulation. But the current gold coins and silver coins of different regions were of the most diverse qualities and denominations. Uniformity was not to be found even within the same district. The resulting confusion led to the demand for a uniform system of currency. After some preliminary steps, the present silver rupee, 180 grains in weight and $\frac{11}{12}$ fine, was established as the standard coin of the whole of British India, under the Act of 1835. But from time to time, *e.g.*, during 1841–52 and 1864–78, there was a reversion to a limited form of the bimetallic standard, the Government being prepared to receive gold mohurs and sovereigns and half-sovereigns at the public treasuries at fixed ratios in terms of the rupee and the ratio being altered now and then.

From 1878 to 1892 the production of silver nearly doubled. The U. S. A. Congress, in order to check the progressive fall in the gold price of silver, required the Government under the Bland Act of 1878 to buy annually between 20,625,000 and 41,250,000 dollars' worth of silver,

and under the Sherman Act of 1890 at least 54 million ounces of silver a year. But, except for a temporary speculative rise in 1890, the price of silver declined heavily from $52\frac{9}{16}d.$ in 1878 to $37\frac{11}{16}d.$ per ounce in 1892. In consequence, the rupee-sterling rate of exchange also fell from 1*s.* 10·351*d.* in 1873–74 to 1*s.* 2·985*d.* in 1892–93. The payment of "home charges" in the latter year amounted to £16,532,215 and required Rs. 26·5 crores. At the rate of exchange prevalent in 1873–74, it would have required only Rs. 17·8 crores. This brought the Government of India face to face with the prospect of growing deficits or increasing taxation. The fall in the sterling value of the rupee also led the European employees of the Government and mercantile firms to demand compensatory allowance, and thereby aggravated the financial situation. And lastly, as the Bengal Chamber of Commerce pointed out in 1892, the progressive fall in the gold value of the rupee had been impeding the investment of foreign capital in India.

In the meantime two international monetary conferences were held, the first in 1881 in Paris and the second in 1892 in Brussels, with the object of arriving at some sort of international agreement for rehabilitating silver in the national currency systems through a limited or unlimited form of the bimetallic standard. But both the Conferences failed. In such a situation, the Government of India in 1892 strongly urged upon the Imperial Government the view that the time had come for seriously considering the question of closing the mints to the free coinage of rupees and introducing a gold standard.

The project of the gold standard.—The Herschell Committee, which was appointed to consider the matter, generally endorsed the views of the Government of India. Act No. VIII of 1893 was passed, which provided for the closing of the mints to the free coinage of both gold and silver. Almost immediately a Notification was issued by which arrangements were made (*i*) for the receipt of gold at the Indian Mints in exchange for rupees at a rate of 16*d.* per

rupee, (*ii*) for the receipt of sovereigns and half-sovereigns in payment of Government dues at the rate of Rs. 15/- for a sovereign, and (*iii*) for the issue of Currency Notes in exchange for British sovereigns at that rate or for gold bullion at a corresponding rate.

In 1898 an Act was passed which authorised the issue of currency notes against gold received in England by the Secretary of State at the rate of one rupee per 7·53344 grains of fine gold plus the cost of shipping gold to India. And under a Notification issued on January 21, 1898, the Secretary of State announced his readiness to sell, until further notice, telegraphic transfers on Calcutta, Bombay and Madras, at a rate not exceeding 1*s.* $4\frac{5}{32}$*d.* per rupee.

It will be noted that the object of the currency reforms of 1893–98 was (*i*) to prevent a further fall in the gold value of the rupee, (*ii*) to familiarise the people of India with the use of gold without forcing it upon them, and (*iii*) to stabilise the rupee-sterling ratio at 1*s.* 4*d.* per rupee with the upper limit at 1*s.* $4\frac{5}{32}$*d.* Obviously the measures were both experimental and transitional. The ultimate aim was the introduction of a gold standard with gold coins and rupees in concurrent circulation at a fixed ratio, the rupee being reduced to the status of full legal tender token money.

In spite of the closing of the mints altogether to the coinage of rupees for five years in the face of growing population and rising export balance, and notwithstanding large borrowings in London, reduction of the drawings of the Secretary of State, and rise of gold prices, all of which tended to keep up the rupee-sterling rate of exchange, the Indian exchange fell steadily away from 1*s.* 4*d.* on June 27, 1893, to 1*s.* $0\frac{31}{32}$*d.* on January 23, 1895. From this latter date, the rate began to rise slowly and steadily for a period of 36 months till in January, 1898, it reached the legal ratio of 1*s.* 4*d.* and afterwards moved steadily around that point. It was at such a time that the Government of India asked the Secretary of State to terminate the period of transition without delay and submitted specific

proposals for further advance towards the gold standard. The Fowler Committee was appointed in April, 1898, to examine the Government of India's scheme and to report on measures calculated to make effective their declared policy of establishing a gold standard in India.

There were two main questions for the Committee to answer: (1) Should there be a reversion to the silver standard with free coinage of rupees? or (2) If it was desirable to adopt a gold standard, should it be backed up by a gold currency in actual circulation or by gold in reserve?

The Committee rejected the suggestion for a return to the silver standard, mainly because such a return would mean a drifting back to the risks and uncertainties of 1878–93, from which the currency and the financial system of India had been rescued after six years of careful management.

As regards the second question, there were three interesting projects for the Committee to consider. There was, first of all, the Government of India's scheme to contract the rupee circulation so as to encourage the importation of gold coins and build up a gold reserve out of the proceeds of the sale of silver bullion, with the ultimate object of introducing a full-fledged gold standard.[1] Secondly, there was the plan of a gold bullion standard suggested by Lesly Probyn, which would (*a*) institute a separate issue of gold notes of the denomination of Rs. 10,000 to be issued in exchange for gold and to be redeemed in rupees or gold at the option of the holder, and (*b*) make the ordinary legal tender notes convertible, at the option of the Currency Department, into sovereigns or gold bars subject to a minimum of £671/- (approximately Rs.10,000/-).[2] The third plan, that of a gold-exchange standard, was submitted by A. M. Lindsay, who suggested that the rupee should be freely convertible into sterling drafts at a rate of $15\frac{3}{4}d.$ per rupee out of a sterling fund to be located in London and that sterling should be freely convertible into

[1] *The Fowler Committee Report*, para. 42.
[2] Ibid., para. 49.

rupee drafts at $16\frac{1}{16}d.$, subject to the condition that the minimum limits for such sales were to be £1,000/– and Rs. 15,000/– respectively.[1]

Judged by modern currency ideas and habits, both these schemes of Lesly Probyn and A. M. Lindsay respectively were certainly more sound and more economical than a gold standard with gold currency in circulation, which the Government of India had in view and the Fowler Committee approved. They were rejected by the Committee because there were no precedents for them and because they were unacceptable to orthodox opinion. Instead the Committee recommended that the British sovereign and half-sovereign should be made legal tender and current coins in India and that the Indian mints should be thrown open to the unrestricted coinage of gold into sovereigns as in the three Australian branches of the Royal Mint. It further recommended that the rate of exchange should be permanently fixed at 1*s.* 4*d.* and that rupees, which should be of restricted coinage and unlimited legal tender, should not be legally convertible into gold, *i.e.*, for internal purposes, but that gold from the reserve should be freely available in exchange for rupees whenever the rate of exchange tended to fall below the gold-export point. It also laid down that the coining of fresh rupees should not be undertaken till such time as gold in actual circulation tended to rise above reasonable proportions and that the profits of future rupee coinage should be set aside in a special reserve.

The coming of the gold-exchange standard.—Under the Indian Currency Act of 1899 the sovereign and half-sovereign were made unlimited legal tender in India at 15 rupees per sovereign. Negotiations for the establishment of a gold mint in India were carried on during the years 1899–1903 but fell through because the British Treasury had raised technical difficulties and because in the meantime the attempt at introducing gold coins into active circulation had failed.[2] The Gold

[1] *The Fowler Committee Report*, para. 52.
[2] Keynes, *Indian Currency and Finance*, pp. 64–66, 73–74.

Standard Reserve was instituted in 1900 out of the profits of the coinage of rupees, which was resumed for the first time since 1893. In 1904 the Secretary of State notified his willingness to sell Council Bills at 1*s.* 4$\frac{1}{8}$*d.* per rupee without limit. In 1908, sterling drafts were sold in Calcutta on London at 1*s.* 3$\frac{29}{32}$*d.* per rupee to the extent of £8 million and cashed out of the Gold Standard Reserve. In the meantime, steps were taken to make the composition and location of the Paper Currency Reserve flexible within certain limits. As a result of these successive steps taken by the Government to implement the recommendations of the Fowler Committee and to meet unforeseen contingencies as they arose, the Indian Currency system, instead of becoming the gold standard as envisaged by the Fowler Committee, came to conform to the Lindsay Scheme of 1898, that is, a gold-exchange standard.

The main characteristics of the Indian Gold-Exchange standard of this period have been explained by Keynes in his classic work, *Indian Currency and Finance*, and may be summed up as follows:—

(1) The rupee was unlimited legal tender, and so far as the law provided, inconvertible into gold, and as such it was sometimes described as inconvertible note printed on silver.

(2) Currency notes of the denominations of Rs. 5, Rs. 10, Rs. 50, Rs. 100, Rs. 500, Rs. 1,000 and Rs. 10,000 were unlimited legal tender and convertible into rupees. The fiduciary issue was fixed at a maximum of Rs. 14 crores, the limit for investment in British Government securities being Rs. 4 crores and the rest of the investment being in Government of India securities. The metallic reserve might be kept in London or in India, in gold coin or bullion, or in rupees or silver bullion, subject only to the limitation that all rupee coins should be kept in India.

(3) Sovereigns and half-sovereigns were unlimited legal tender in India at the rate of Rs. 15 per sovereign.

(4) As a matter of administrative practice, the Govern-

ment of India were willing to give sovereigns for rupees at that rate, but the practice was sometimes suspended.

(5) As a matter of administrative practice, the Government were willing to sell rupees or rupee currency, payable in Calcutta or Bombay, in exchange for gold or sovereigns or sterling tendered in London, at the maximum rate of 1*s.* $4\frac{1}{8}$*d.* per rupee. This was known as the sale of Council Bills.

(6) As a matter of administrative practice, the Government were willing to sell gold or sovereigns or sterling, payable in London, in exchange for rupees tendered in Calcutta or Bombay, at the minimum rate of 1*s.* $3\frac{29}{32}$*d.* per rupee. This was called the sale of sterling drafts or Reverse Councils, because the object and procedure of such sale was exactly the reverse of that of sale of Council Bills.

It will be observed that Nos. 5 and 6 were the vital parts of the mechanism of the Gold-Exchange standard, by which the local currency and the international currency were freely convertible into each other for remittance purposes at approximately fixed rates. In order to convert the local currency into international currency, there was one principal fund, *viz.*, the Gold Standard Reserve, which was supplemented by that portion of the Paper Currency Reserve which was located in London and also by the Cash Balances of the Secretary of State for India. On the other hand, in order to convert the international currency into local currency, there were three corresponding funds in India, *viz.*, the Rupee portion of the Gold Standard Reserve, the Indian portion of the Paper Currency Reserve, and the Cash Balances of the Government of India. And although this currency system was evolved, not in obedience to the narrow and dogmatic doctrines enunciated by the Fowler Committee but through gradual adaptation to circumstances as they arose, nearly all students of currency theory and history are agreed that this currency system, by its flexibility and adaptability, had well answered the needs of India, and that it was, in

many respects, a better mechanism than the orthodox type of the gold standard which was recommended by the Fowler Committee and which was repeatedly demanded by public opinion in India.

In April, 1913, a Royal Commission was appointed under the Chairmanship of Austen Chamberlain to examine the mechanism of Indian currency and exchange and to suggest measures for its improvement. In their Report issued in February, 1914, the Commission generally approved of the measures taken by the Government for stabilising the rupee-sterling ratio of exchange, and made important recommendations regarding the various aspects of the use of gold as currency, the minting of gold in India, the development of the note issue, and the location and utilisation of the balances and the reserves. But before these recommendations could be considered and acted upon, the War broke out and threw the currency mechanism once again into the melting-pot.

The War and the breakdown of the gold-exchange standard.— The outbreak of the War in August, 1914, caused a dislocation of trade and industry and a temporary loss of confidence. The exchange weakened; there was a demand for withdrawal of savings banks deposits and encashment of notes; and there was a run on the Indian gold stocks. By prompt action such as sale of Reverse Councils, announcement by the Government of their intention to provide adequate and continuous remittance facilities, and ready encashment of notes in gold and in rupees, general confidence was soon restored. And normalcy was brought about by February, 1915. The currency mechanism continued to function smoothly till the end of 1916, when difficulties of an exceptional nature cropped up.

On the one hand, India's heavy trade balance, large disbursements on behalf of His Majesty's Government and certain Dominions and Colonies, and the inability of foreign countries to liquidate India's trade balance in terms of precious metals caused an extraordinary demand for rupee currency, which was partially met by purchase

of silver for coinage to the extent of 538 million ounces, inflation of paper currency almost to the point of inconvertibility, and other supplementary measures designed to reduce the extra-legal facilities for encashment of notes. The rest of the world, too, bought silver on a large scale for coinage purposes. On the other hand, world supply of silver fell by some 50 million ounces per annum by reason of political disturbances in Mexico. The consequence was a rapid rise in the price of silver. The highest price in 1915 was 27¼*d.* per ounce. But it rose by stages to as much as 78*d.* per ounce on December 17, 1919. It was impossible for the Secretary of State for India to sell Council Bills at 1*s.* 4*d.* per rupee without loss when the price of silver exceeded 43*d.* per ounce. To avoid this loss, therefore, the rate for Council Bills was raised from time to time according to the rise in the sterling price of silver till on December 12, 1919, the rate for Council Bills rose to 2*s.* 4*d.* per rupee.

There was thus a departure from the Gold-Exchange standard, because condition No. 5 as stated on page 223 was broken, and it was broken not because there was difficulty in giving gold or sterling for rupees, but because there was difficulty in giving rupees in exchange for international currency at fixed rates. Further, to check the demand for Council Bills and to mobilise the exchange resources for financing essential exports, large measures of exchange control were enforced. Moreover, to strengthen the Paper Currency Reserve and to supplement the supply of rupees, Government compulsorily acquired all gold imported into India and issued gold bullion, 15-rupee gold mohurs and sovereigns to the extent of £18 million. And, finally, to facilitate the issue of sovereigns, a branch of the Royal Mint was established in Bombay in August, 1918.[1]

To examine the situation brought about by the break-up of the gold-exchange standard, the Babington Smith Committee was appointed in May, 1919. The main task that was laid on the Committee was to suggest a

[1] *Babington Smith Committee's Report*, paras. 25–27.

rate of exchange between the rupee and gold which could be stabilised without placing any financial burdens on the Government. It was admittedly a difficult task, because the future price of silver in terms of gold was thoroughly uncertain. On the one hand, it was possible that with the return of peace, the supply of silver from Mexican mines would increase and thereby tend to lower its price. On the other hand, there was a probability that China and the U.S.A. would continue to be large buyers of silver and thereby tend to keep up its price. The Committee, however, rather rashly assumed that silver would continue to be dear for some time to come and put the future price at 62·9*d.* (gold) per ounce. On this assumption regarding the future price of silver, the alternatives open to it for stabilising the exchange value of the rupee were three, namely, (*a*) to fix the rate of exchange at 2*s.* gold so that the rupee might not be externally over-valued, (*b*) to fix a lower rate of exchange and debase the rupee, or (*c*) to declare the notes inconvertible. It rightly rejected (*b*) and (*c*), as either of these measures was sure to shake public confidence in the stability of the currency, specially under the peculiar circumstances of India. Consequently, it recommended the first alternative, *viz.*, that the rupee should be stabilised at 2*s.* (gold) or Rs. 10 per sovereign.

The 1920–21 episode.—The Report was signed on December 22, 1919, and issued in February, 1920. And the Committee's recommendations were accepted by the Secretary of State for India. The publication of the Report led to a keen demand for remittances to London, mainly on account of the fact that European businessmen, who had accumulated their profits in India during and after the War, now saw a favourable opportunity of remitting their funds to London. By June, 1921, the trade balance became unfavourable. World prices also began to fall. The demand for imports became particularly strong, while exports shrank off. The combined result of all these factors was a persistent demand for sterling drafts, which the Government continued to sell at rates ranging from 2*s.* $3\frac{29}{32}$*d.* (sterling) to 2*s.* $10\frac{29}{32}$*d.*

(sterling). The attempt to hold the rupee at 2*s.* (gold) was not successful, because the market rate of exchange was falling fast. From June, 1920, therefore, the Government tried to maintain the rupee at 2*s.* sterling. This attempt, too, failed, and was abandoned on September 28, 1920. World prices continued to fall, but it was not possible to deflate Indian currency to the necessary extent so as to cause Indian prices to fall *pari passu* with world prices, because there was a succession of deficit budgets which were largely met by borrowing from the Paper Currency Department against Treasury Bills. The result was a continuous fall in the rate of exchange, which sank to $11\frac{9}{32}d.$ gold or 1*s.* $3\frac{13}{32}d.$ sterling in July, 1921. The policy of the Government was to allow the exchange largely to respond to world conditions so as not to disturb unduly the Indian price structure. This might be called the policy of "flexible" exchange, a policy which has been followed by England during the recent depression. By January, 1923, the tide definitely turned and exchange began to rise till it reached the level of 1*s.* 4*d.* gold or 1*s.* 6*d.* sterling in October, 1924. From that date to July, 1926, the upward tendency of the exchange was kept in check by free purchases of sterling.[1]

The currency episode of 1920–21 has been a subject of controversy in India. As already explained on page 226, it was out of the range of practical politics for the Government to resolve the silver difficulty by declaring the note issue inconvertible or by debasing the rupee. Nevertheless, in view of the admitted uncertainty about the future price of silver and about the dollar-sterling exchange rate, it is arguable that the Government should have waited for developments and allowed the exchanges to take care of themselves till world conditions showed some signs of stability. Had the Committee and the Government kept an open mind, it would not have been extraordinarily difficult for them to foresee that Indian exports were likely to fall off and imports to rise rapidly in the near future, because it was a known fact that there

[1] *Hilton Young Commission's Report*, para. 8.

had been abnormally large exports and abnormally small imports in the preceding years, and that while the outside world had been overstocked with Indian goods, India had been starved of essential imports. It was also known that European companies in India had accumulated vast profits in the War period, which were waiting to be remitted abroad with the return of normalcy. Hence it appears that while the Committee reckoned at a high rate the probability of the price of silver ruling high, it took little account of the probability that it might fall or that there might be an adverse balance of trade and a strong demand for outward remittance of funds. It would, therefore, be a fair criticism to say that, when the probability of exchange movement in either direction was equally strong, the most reasonable course of action for the Committee to recommend and for the Government to adopt was to continue the policy of flexible exchanges for a further period till things began to take a more definite shape than was the case in 1919–20.[1]

II. The 18*d.* Ratio and the Gold Bullion Standard: 1925–31

The ratio controversy of 1925-27.—England returned to the gold standard in May, 1925. In the following August a Royal Commission was appointed under the Chairmanship of Edward Hilton Young to examine and report on the Indian exchange system and currency and to make necessary recommendations. The Commission's task was threefold: (1) to find out the appropriate rate for stabilisation of the exchange; (2) to make recommendations regarding the system of currency and exchange, and (3) to recommend measures for the establishment of a Central Bank as the currency authority of the country.

As on previous occasions, in 1925–26, too, the appropriate parity between the rupee and gold was the subject of a keen controversy. The majority of the Commission

[1] See the *Report of the Babington Smith Committee*, paras. 34, 42, and 58; Appendices to the *Report of the Royal Commission on Indian Currency and Finance*, Vol. III, p. 443, memorandum by C. H. Kisch, and specially pp. 602–03, memorandum by Gustav Cassel.

recommended stabilisation at 18*d.* gold, mainly on the ground that this had been the *de facto* rate for the preceding twelve months, June, 1925 to June, 1926, and that by the latter date Indian prices had become substantially adjusted to world prices as well as to internal wage-structure.[1] The minority of one, Sir Purshotamdas Thakurdas, who represented the opinion of the Indian business community, held that the 18*d.* ratio had been brought about by deflation from July, 1924, to May, 1925, during which period the rupee price level fell from 176 to 160 and the rate of exchange rose from 16*d.* to 18*d.* gold, and that, consequently, the rupee should be stabilised at 16*d.*, which had been the *de facto* and *de jure* ratio for nearly twenty years, 1898–1917. He also pointed out that during 1924–26 the Government had deliberately set out to contract, or at any rate to prevent legitimate expansion of, Indian currency, which had been responsible for the sharp rise of exchange from 16*d.* to 18*d.* in the course of a year.[2]

There are two questions that arise out of this controversy. First, would it have been appropriate for the Government to stabilise the rupee at 16*d.* gold in September, 1924, when the Legislature asked for it? Second, when the relevant economic facts became as they did in 1926–27, was the 18*d.* ratio a proper one? Now, by September, 1924, the only important country that had stabilised the exchange was Germany, while all other countries, including the United Kingdom, had yet to stabilise their exchanges. Consequently, in so far as the Government of India refused to fix the legal gold parity in 1924, they acted wisely. But, according to the evidence recorded by the Commission, the exchange value of the rupee had been fairly stable round 1*s.* 3*d.* gold for a period of 18 months, December, 1922, to June, 1924.[3] Meanwhile, strenuous efforts were being made by the Government to contract currency so as to allow the rate to rise. The rate rose to 16*d.* gold in September, 1924, when the Legislative

[1] *Report of the Royal Commission*, op. cit., paras. 168–93.
[2] *Minute of Dissent*, by Sir Purshotamdas Thakurdas, paras. 66–97.
[3] *Report*, op. cit., para. 182.

Assembly formally asked the Government to stabilise the rupee at that point. Since there was no other country in the world that took special pains to raise the exchange rate even above the pre-war parity, and since the utmost that was demanded by financial orthodoxy was that the stabilisation should be at the pre-war gold parity, the only reasonable course for the Government to follow was to allow the ratio to remain at 1*s.* 4*d.* gold, as certainly it would have remained if they had desisted from active measures for prevention of legitimate currency expansion.[1] What seems to have happened is as follows: In June, 1924, the pound sterling was at 88·8 per cent of the pre-war gold-parity. Having decided to raise the dollar-sterling rate to the pre-war gold-parity, the British monetary authorities resorted to a considerable dose of deflation. In consequence, the sterling price index fell from 163 in June, 1924, to 149 in February, 1926, *i.e.*, a fall of about 9 per cent. The Indian authorities, too, probably in order not to be left behind their masters in the enterprise of deflation, effected a corresponding deflation in India. The Indian price index number fell from 176 to 157 (Calcutta index), *i.e.*, by 11 per cent, and the rate of exchange rose from 1*s.* 4*d.* to 1*s.* 6*d.* gold, *i.e.*, by 12½ per cent. If India had kept the rupee-gold parity at 16*d.*, while England was raising the sterling-gold parity by deflation, there would have been no fall of general index numbers of prices in India, and consequently no disturbance to the internal economic stability that was being painfully attained since 1921. Nor is there any good reason to suppose that England's exports to India would have shrunk, thereby increasing the deflationary burden on her industries. For the rise in the sterling-gold parity by some 12½ per cent was accompanied by deflation and fall of sterling prices, so that the disadvantage of the higher gold-ratio would have been largely counter-balanced by the advantage of lower prices in so far as the export trade was concerned. In this view of the matter, one can unhesitatingly state that the Indian authorities had no justification whatsoever

[1] *Minute of Dissent*, op. cit., para. 76.

for deflating the Indian currency during this period in order to raise the rupee-gold ratio from 16*d.* to 18*d.* Even granting that the subsequent developments in the theory and practice of exchange and currency regulation could not have been foreseen by them, it would be a just criticism of their action to say that there was absolutely no ground for their going beyond the limit which was then demanded even by the most orthodox financial views, namely, that stabilisation should be effected at or near the pre-war gold-parity.

We should now turn to the position in 1926–27, when the Royal Commission reported and the Government legalised the rupee-gold ratio at 1*s.* 6*d.* By the date the Commission reported, namely, July 1, 1926, the 18*d.* gold ratio had been stable for over a year, and by March, 1927, when the Currency Act was passed, for over 21 months. During this period, Government had, of course, actively intervened both to prevent a rise and a fall of the ratio beyond the gold-points. Nevertheless, during this period, both world prices and Indian prices remained fairly stable. India's export trade considerably revived, and general economic conditions, on the whole, appeared to be fairly normal. Consequently, though it was a wrong policy that had brought about the facts as they became in 1926–27, there was nothing to be gained and perhaps something to be lost by trying to lower the ratio of exchange to 16*d.*, which would have caused an inflation and perhaps a disturbing boomlet.

Gold bullion *versus* gold-exchange standard.—As regards the mechanism of currency and exchange, the Commission rejected both the sterling-exchange and gold-exchange standards and recommended the adoption of the gold bullion standard. Their main objection to the exchange standard was that it was not simple and intelligible to the general public, because the right to convert the internal token money into gold was too abstract and because its mechanism was too refined and complicated. On the other hand, according to the Commission, the supreme merit of the gold bullion standard as against

the gold-exchange standard was that it would not only be stable, but simple and certain as well, because the right of converting the token currency into gold would be based upon law and not upon administrative discretion expressed through a whole series of cumbrous regulations and notifications.

But this comparison between the relative merits of the two systems was an extremely superficial and misleading one, scarcely worthy of an expert body like a Royal Commission. For recent studies have shown that even the pre-war gold standard was not so simple and automatic as it was imagined to be. London, and to a minor degree other important financial centres, had to "manage" the gold standard to a certain degree in order that it might function smoothly and beneficially. It is also known to us that much that was simple, automatic and intelligible in the working of the gold standard was sometimes gravely harmful to economic stability, and that its awkward and disturbing consequences had to be warded off by frequent "management," which was neither simple nor intelligible. Moreover, under the gold bullion standard, it was provided that gold bullion would be supplied in exchange for legal tender token currency in quantities not less than 1,065 tolas and at prices to be strictly determined by the position of the exchange between the gold points, so that the currency authority would be responsible for supplying gold bullion for monetary purposes alone. This system of convertibility, too, like that of the exchange standard, would be of direct concern only to bankers and merchants connected with the financing of foreign trade, and intelligible to them, and not to the uninitiated general public. Furthermore, under the gold bullion standard as actually adopted under the Currency Act of 1927, the currency authority was laid under an obligation to buy and sell gold or gold-exchange *at option* at statutory or notified prices. Consequently, there was little substantial difference between the legal obligation laid on the currency authority to buy and sell gold or gold-exchange at approximately fixed prices and the habitual, though discretionary, policy

of buying and selling gold or gold-exchange that was actually followed by the currency authority under the exchange standard. The Commission knew, too, that the gold-exchange standard, with some minor modifications in practice and operated by a Central Bank, would be "as automatic as, and no more subject to manipulation than, the system of the United States of America or Great Britain."[1] And, finally, it would be no conclusive argument for the rejection of the exchange standard that it had broken down during and after the war. For the gold standard, too, broke down under the strain of the World War and again during the depression. And experience has abundantly shown that no currency standard, however solid its basis, can remain unshattered, far less intact, in abnormal situations, national or international. Here, too, therefore, it would be legitimate for one to suspect that the Hilton Young Commission had already made up their mind in favour of the gold bullion standard which had just been introduced in Great Britain, and that, consequently, they were unable to examine the question of the Indian currency system with an open mind.

III. The Currency Policy of India during the World Economic Depression, 1931–38

The problem of the standard and the ratio.—When England left the international gold standard in September, 1931, India followed suit and linked up the rupee with the pound sterling at 18*d.* under Executive Orders. Criticism of the Government action has centred mainly round three points, *viz.*, (*a*) the sterling link, (*b*) the 18*d.* ratio, and (*c*) Government non-intervention in regard to gold exports on a large scale.

With regard to the standard, Government had three alternatives open to them, namely, (*a*) to keep to the gold standard, (*b*) to remain on an independent standard, and (*c*) to adopt the sterling link. Now, the abandonment of the gold standard was forced on the greater part of the world by large maladjustments in economic and financial

[1] *Report*, op. cit., para. 28.

structure, and as the history of the last seven years has shown, no country could remain on the gold standard unless it had abnormally large gold reserves like the U.S.A. Even if India had remained on the gold standard in September, 1931, it was a question of a few years before she, like France and other gold-bloc countries, would have been forced to give it up. Again, as a debtor country with large foreign obligations, with her export trade exposed to various trade barriers, and with no Central Bank, it would have been impossible for India to remain on an independent standard. And, since the gold standard had to be ruled out, the only alternative left to her was the sterling standard with its large area, which had the advantage of stabilising her foreign obligations, a large part of her foreign trade, and by far the greater section of her external banking and financial connections. In any case, her almost instinctive adoption of the sterling link has been abundantly justified by the subsequent course of events and also by the fact that the management of the sterling standard has been the most outstanding instance of skilled and successful monetary management in modern times.

But the adoption of the sterling link would not necessarily mean the maintenance of the 18*d.* ratio. It is indeed true that the linking of the rupee with the pound sterling meant an automatic depreciation of the rupee in terms of gold to the extent of over 30 per cent. It is also true that the 18*d.* ratio kept her sterling obligations, called Home Charges, unaltered in terms of rupees. But the very significance of the abandonment of the gold link lay in the fact that thereby the countries concerned acquired the autonomous power to insulate the internal economic structure against the disturbing effects of external economic and financial forces by flexible parities of exchange so adjusted from time to time as to absorb the shock of external forces more or less completely. This is largely what Great Britain herself has been doing during the last eight years, and France since October, 1936. As Keynes has explained, and as recent currency policies all the world over have shown, there is no hard and fast rule by which we can

find out the equilibrium rate of exchange between two or more paper currency standards. It has to be discovered tentatively from time to time in the light of internal cost-price relations, profits, unemployment, movements in the terms of trade as reflected in the index numbers of export and import prices, balance of trade, and gold movements on trade account.[1] Judged by these tests, all available data clearly indicate that the rupee was over-valued during the whole period of the depression: Thus, taking 1928 to be the base year, while the lowest level of price index reached in England (1932) showed a fall of 36·3 per cent (the *Economist* index), the lowest level of wholesale price index reached in India (1933) showed a fall of 40 per cent (Calcutta index). Again, whereas by 1936 the wholesale price index in England recovered to the extent of 16·3 per cent, the corresponding figure for India was only 5·7. A similar indication of the over-valuation of the rupee in relation to commodities is given by the figures of aggregate profits of certain representative industries. These aggregate profits fell from Rs. 10,90 lakhs in 1928 to Rs. 9,46 lakhs in 1929, Rs. 4,96 lakhs in 1930, Rs. 2,60 lakhs in 1931, which was the low-water mark and from which they slowly recovered to Rs. 3,64 lakhs in 1932, Rs. 4,39 lakhs in 1933, Rs. 5,51 lakhs in 1934, and Rs. 5,90 lakhs in 1935.[2] Again, like all other agricultural countries, India also suffered from a worsening of the terms of external trade, because the prices of her exports fell more heavily than the prices of imports. For, between 1927–28 and 1933–34, while the index number of export prices fell by 46·5 per cent, that of import prices declined only to the extent of 34·8 per cent, though, it should be noted, this discrepancy was increasingly narrowed down in the subsequent years.[3] This worsening of the terms of trade was counteracted by most agricultural countries such as Australia, New Zealand, Brazil, Argentine Republic and Denmark by a depreciation of the exchange. There can be little doubt that India, too, might have

[1] Keynes, "The Future of the Foreign Exchanges," *Lloyds Bank Monthly Review*, October, 1935.
[2] *Review of the Trade of India*, 1936–37, pp. 17–19.
[3] Ibid., p. 22.

profitably followed such a course so as to relieve acute distress among her agricultural population.[1]

Gold exports, their causes and effects.—A third point of criticism of the Government currency policy arises out of the unprecedented exports of gold from India since October, 1931. It has been estimated that from 1493 to 1931 India imported gold to the extent of 157·7 million ounces valued at Rs. 900 crores. During the six years 1931–37, however, she exported gold to the extent of 35·4 million ounces valued at over Rs. 298 crores. That is to say, in six years alone she exported between one-fourth and one-fifth of the entire stock of gold she had patiently accumulated through a period of 438 years.[2] And this was undoubtedly a startling state of affairs.

This matter of gold exports has been discussed in the next following chapter of this symposium by another writer, who largely attributes the export of gold to the rupee-sterling link and to the under-valuation of the rupee in terms of sterling. That line of interpretation is partly right from the narrow technical point of view and would seem to be supported by the figures of purchasing-power parities based on wholesale price index numbers or cost of living index numbers. Thus, according to the calculations made in the *League of Nations' Report on Commercial Banks*, 1929–34, Table XVII, p. lxxiv, the extent of under-valuation of the rupee in terms of sterling during 1931, 1932, 1933 and 1934, respectively, was 10·31 per cent, 15·04 per cent, 16·18 per cent and 18·23 per cent. And, according to the League's Monetary Review for 1936–37, p. 38, the corresponding depreciation of the rupee in December, 1934, December, 1935, December, 1936, and March, 1937, respectively, was 23·45 per cent, 20·48 per cent, and 31·38 per cent. According to the present writer's calculation, the

[1] Cf. Dey, "The Rupee-Ratio Controversy," the *Modern Review*, May, 1937.

[2] Figures taken from Kitchin's estimate, *Interim Report of the Gold Delegation to the League of Nations*, p. 80, and *Report of the Reserve Bank of India on Currency and Finance*, 1935–37, p. 47.

under-valuation during the period ranged between 10 and 28 per cent.

But this view of the matter is rather defective in several respects and has been rejected by many leading economists, whose opinion is very well expressed by Haberler when he says that "Measurements of 'purchasing-power parity' based on comparisons of price levels or of changes in price levels in both countries afford only very rough and unreliable criteria of over- and under-valuation."[1] Moreover, if under-valuation in this context were the main cause of gold exports, these would have gone on increasing year by year instead of decreasing as they have actually done, for a comparison of prices and costs of living in England and India shows a progressive depreciation of the rupee in terms of sterling and gold. On the other hand, it is seen that there has been a continuous decline in the export of gold with improvement in the balance of trade, rise of prices, and narrowing down of the discrepancy between import and export prices.[2]

We are, therefore, inclined to explain the export of gold largely as follows: There was acute economic distress among the peasants and zamindars due to disastrous fall of agricultural prices, which led to their savings in the form of gold hoards being drawn upon on a large scale. But, (*a*) due to the ignorance of the villagers about the world price of gold, (*b*) pressure of intensive propaganda on the part of bullion dealers in the upcountry centres causing quick dishoarding, and (*c*) distress sales,[3] the internal price of gold at which it was bought by the bullion dealers was low as compared to the world price.[4] Consequently, the export of gold became highly profitable for the bullion dealers. On the other hand, as economic conditions gradually improved due to the rise of prices and increase of exports, the distress was mitigated, dishoarding of gold

[1] Haberler, *Prosperity and Depression*, p. 334.
[2] See Dey, "The Rupee-Ratio Controversy," the *Modern Review*, May, 1937, and the *League of Nations' Monetary Review*, 1936–37, p. 61.
[3] *Report of the Controller of Currency*, 1932–33, p. 9.
[4] Cf. Adarkar, "Gold Export Fallacies," *Indian Journal of Economics*, January, 1936, pp. 295–98.

declined, the disparity between the internal and external prices of gold became less and less, and gold export began to diminish, even though the depreciation of the rupee in terms of sterling and gold remained great or kept on increasing. This line of interpretation is entirely in accord with the outstanding facts of world gold movements from the end of 1932 to September, 1936. In this period, large amounts of gold were secured by the U.S.A., the United Kingdom, Sweden, Norway, South Africa, Portugal, Egypt, Finland and Belgium, which had adjusted their currencies by devaluation or depreciation, while considerable quantities were lost by the Netherlands, Switzerland, Italy, and most heavily of all by France, which were still on the gold standard and which, therefore, failed to devaluate or depreciate their currencies.[1]

In this view of the matter, the large exports of gold from India during the depression must be regarded as having been caused by acute economic distress rather than by external under-valuation of the rupee. Moreover, gold and land are the two forms in which wealth is stored in India, and they are sold only in the last extremity of distress, and not on account of the profit motive, though, of course, the profit motive stimulated the bullion dealers to collect and export this gold on a large scale. This may be restated in technical terms by saying that the rupee was internally over-valued in terms of gold and other commodities. It was this internal over-valuation of the rupee in terms of gold and commodities, *i.e.*, too low internal prices of gold and commodities, that caused the apparent external under-valuation of the rupee in terms of the pound sterling. Had a rise in Indian prices of gold and commodities been brought about by a proper degree of inflation, the rupee's internal over-valuation would have been checked and its external under-valuation in terms of gold and the pound sterling largely eliminated, and gold exports would have been minimised.

But our conclusion that the exports of gold were caused by the failure of the Government to raise prices in India

[1] Vide the *League of Nations' Monetary Review*, 1936–37, pp. 62–66.

does not mean that the effects of these exports were bad for India. For these gold exports caused by low prices were one of the means, though certainly not the best means, of relieving distress and raising price levels and thereby, though in a roundabout manner and with an unnecessary time-lag, removing the causes of the exports. As we have stated on page 236, during the period 1931–37, gold exports amounted to 35·4 million fine ounces valued at over Rs. 298 crores, which meant a profit of about Rs. 99 crores over the purchase price. And this sum of Rs. 99 crores was obtained by the bullion dealers, exporters, peasants and zamindars between them. Had the people in distress no gold to sell at a profit, they would have been compelled to sell their lands, cattle and other possessions at a loss and would thus have been deprived of the very means of their livelihood. Moreover, the sale of gold meant conversion of dead assets into purchasing power or active capital, which was invested in Treasury Bills, bank deposits and postal cash certificates and which served to bring down the rate of interest on gilt-edged securities and other long-term investments and thereby stimulated industrial expansion and building activities on a large scale. It has also helped India to reduce her external debts to a considerable extent, as shown by the following: During the period 1923–31, India's balance of account was credited with Rs. 93 crores, which might have been utilised to reduce her foreign obligations. But, instead, she borrowed Rs. 130 crores more in order to buy gold worth Rs. 223 crores. On the other hand, in the period 1931–34 she had an international debt burden of Rs. 105 crores, and yet she not only liquidated this debt but also reduced her external obligation by a further amount of Rs. 75 crores, by exporting gold to the value of Rs. 180 crores. It is estimated that during the period 1493–1931 she imported gold to the extent of 157·7 million ounces valued at Rs. 900 crores. If she had only cut down her gold imports by half, her entire external debt would have been wiped off, and the greater part of the "drain" of wealth would have been eliminated.

Gold exports and governmental non-intervention.—It was also suggested in some quarters that the Government should have acquired all the gold to strengthen their reserves. What actually happened was that the exporters sold the gold abroad and obtained sterling funds and securities to the extent of Rs. 300 crores. The Government bought a large part of this sterling to meet their English charges, to extinguish some part of their foreign debts, and to increase their holdings of sterling securities from about Rs. 32 crores to Rs. 78 crores. At the same time, the gold reserves were strengthened by acquisition of gold valued at over Rs. 16 crores in India. Had the Government acquired all the gold, the result would have been, on the one hand, that the entire note issue would have been covered cent per cent by gold (Rs. 208 crores), and, on the other, that there would have been sale of Rs. 102 crores worth of sterling and rupee securities from the reserves.[1] In view of the uncertainty of the future price of gold and of the gold standard, this course of action would have been speculative in the highest degree, and would have entailed the loss of revenue derived from the securities. It is true that both the U.S.A. and the United Kingdom have accumulated large gold reserves at high costs during the depression. But all students of recent monetary conditions know that it has now become a grave problem for these two countries to decide what should be done with these costly gold stocks. Moreover, should there be a general return to the international gold standard, and should India then decide to replace the securities by gold, it would be the easiest thing for her to convert the sterling securities into gold.

Further, the accumulation of unwanted gold stocks in the United Kingdom, the U.S.A. and to a certain extent in France actually means that these three wealthy nations are at present carrying the burden and the risks of world's gold, and that they will ultimately have to part with their surplus gold stocks so as to facilitate a return to the gold

[1] For figures, see *Reports of the Controller of Currency*, 1931–32 to 1934–35, and *Report of the Reserve Bank of India on Currency and Finance*, 1935–36 and 1936–37.

standard. Moreover, as we have already pointed out, the skilful management of the pound sterling and the holding of large gold stocks in the United Kingdom have so strengthened the position of the pound sterling that, as international currency it commands a prestige which is at least as high as that of gold. And, finally, since, for political, financial and psychological reasons, the United Kingdom and the U.S.A. are not only the holders of the greater part of the surplus gold reserves of the world but also the two outstanding buyers of gold, and since the production of new gold has increased enormously in recent years under the stimulus of high price, the future price of gold will largely depend upon the decisions of these two countries: If they can continue their present expensive policies, its price will continue high; but if they give up the policy of buying unwanted gold, its price will appreciably fall. It would, therefore, appear that the policy that has been actually followed by the Government of India with regard to gold has been the wisest under the circumstances of the case.

A second suggestion which originated from the representatives of Indian Commerce was that a duty should be levied on gold exports. This suggestion also was turned down by the Government of India on the ground that it would ultimately fall on the sellers of gold, who as a rule were poor persons with small stocks of gold. Most of this gold was bought and hoarded by people of Europe or by European Central Banks which converted foreign exchange reserves into gold due to lack of confidence in the stability of currencies. Consequently, the demand for this gold on the part of the Western countries was largely inelastic. That being so, the foreigners would have borne a part of the duty. The rest of the duty would have been shared between the exporters, upcountry distress sellers and substantial investment sellers. And in so far as the "the distress sellers" were concerned, their supply was inelastic, and bargaining position weak as against bullion dealers, and, therefore, they would have probably borne a part, perhaps a large part, of the duty. In this view of the matter, there-

fore, the Government were justified to a certain extent in refusing to levy an export duty on gold.[1]

Postscript, July 31, 1938.—The problem of the equilibrium ratio between the pound sterling and the rupee is still an unsolved one. Due to the weakness of the export trade, the rupee weakened towards the lower exchange point of 1*s.* $5\frac{49}{69}$*d.* from April, 1938, onwards, and the demand for devaluation of the rupee was revived. Early in May the French franc was again devalued to 178 francs to the pound sterling, and the demand for the devaluation of the rupee became stronger. The Working Committee of the Indian National Congress, which is the greatest political party in the country and which controls the Government in seven out of the eleven Provinces, at their meeting held in Bombay, declared that the rupee should be devalued and that all pressure should be put upon the Government of India to devalue the rupee. Early in June, the Government of India issued a *communique* to the effect that they were not going to alter the rupee-ratio and that they had ample resources to defend the rupee. But, since Indian prices are still far lower than those of other countries of the world, including agricultural countries like Australia, Canada, Argentine Republic, since the distress caused among the peasants by abnormally low prices of staple crops is still acute, since the cost-price disequilibrium still continues and recently led to a series of wide-spread industrial strikes throughout India, and since the Provincial Governments are still hovering anxiously and fearfully on the brink of financial disequilibrium and are faced with the undesirable and unpopular alternatives of retrenchment or taxation, both of which are doubtful remedies of the consequences of a prolonged depression, the present writer holds that there is a *prima facie* case for devaluation of the rupee and that it is incumbent upon the Government of India to have the matter thoroughly investigated by a body of experts, specially because their currency policy in the

[1] Cf. J. C. Sinha, "Currency Events during the Depression," *Calcutta Review*, January and February, 1938.

past has been deservedly subjected to strong public criticism.

IV. The Future of Indian Currency

Trade cycle and monetary policy.—It is now being increasingly recognised in theory and practice that money plays an important part in the genesis and development of those cycles of booms and depressions which constitute one of the major economic problems of modern times. And the theory of monetary management, tested by practical experiments in recent decades, and specially during the post-war reconstruction and again during the depression, has now arrived at a stage when it is possible to sketch out the main outline of an ideal monetary system in the circumstances of the post-war world.

Now, there is a large measure of agreement among all schools of economic thought that the main objective of monetary policy should be to mitigate, and if possible to eliminate, trade cycles by appropriate regulation of the monetary mechanism. It is also generally agreed that in a slump the best correctives are a cheap money policy operated through the bank rate, open market purchase of securities and a public works programme. But there is a fundamental divergence of opinion among two leading schools of thought as to the most appropriate policy in a boom: One school, represented, among others, by Hayek and Lionel Robbins, suggests that dear money policy is the best cure for a boom.[1] The other school, of which the leading exponent is Keynes, thinks that a dear money policy not only checks the expansion of certain industries beyond the limits of safety, but also prevents the fuller development of other industries as well; and that, moreover, dear money soon produces a state of pessimism among the entrepreneurs and thereby not only checks further development but also causes the collapse of the whole structure, and thus swings back the economic system from

[1] Vide Hayek, *Prices and Production*, second edition, p. 125, and Robbins, "How to Mitigate the Next Slump," *Lloyds Bank Monthly Review*, May, 1937.

the higher plane of fuller activity and employment to the lower plan of stagnation and unemployment, with disastrous consequences to the society.[1] Keynes, therefore, rightly suggests that even in a boom a cheap money policy should be continued, but also that such a policy should be coupled with a large measure of State control over investments so as to check undue or disproportionate development of certain industries making production goods, *e.g.*, steel and engineering industries, the instruments of control being high taxes on Stock Exchange transfers of stocks and shares and discriminate rationing of credit.[2]

Objectives of monetary policy.—But monetary policy should not stop at merely mitigating booms and depressions. Its ultimate aim should be to help in eliminating trade cycles altogether. Monetary factors alone, of course, are not the only causes of the trade cycle. There are certain serious flaws in the mechanism of the individualistic and competitive economic régime, in which ignorance, gambling and mass hysteria also play a decisive rôle and which can perhaps be remedied by a large measure of State regulation and control of investment activities.[3] But those imponderables in the operation of the economic system can also be partly overcome by monetary policy.

Now, in this connection, it has been suggested that a policy of stable prices with money incomes fluctuating directly with productivity or a policy of constant money incomes with prices fluctuating inversely with productivity would serve to remove those uncertainties regarding the prospects of profits, those disparities between production and consumption, and also those arbitrary changes in the price-income structure, which are some of the root causes of trade cycles.[4] A policy of constant money incomes will

[1] Vide Keynes, *General Theory*, pp. 321–24.

[2] Vide Keynes, "How to Avoid a Slump," *The Times*, January 12, 13 and 14, 1937.

[3] Vide Keynes, *General Theory*, p. 164. Also Cf. Dey, "The Rôle of Monetary and Investment Factors in Trade Cycles," the *Indian Journal of Economics*, April, 1938.

[4] Vide Keynes, *General Theory*, pp. 257–71, and Erik Lindahl, quoted by Brinley Thomas, *Monetary Policy and Crises*, pp. 76–78.

mean that the supply of money also should be constant over short periods and should only increase with the slow increase of population and other productive factors over long periods. This, in brief, is the substance of what Hayek means by "neutral money." A policy of constant price levels, on the other hand, will mean that money income should rise and fall with increase or decrease of productivity, and will, therefore, demand that the supply of money should vary accordingly. And this, in essence, is the modern doctrine of "elastic money," which is favoured by Fisher, Keynes, and their followers. Either the one or the other policy having been chosen (and each has its advantages over the other), it will not be exceedingly difficult to prepare appropriate index numbers for measuring changes in the productive efficiency of the factors.

There is also a large measure of agreement that a secondary objective of monetary policy should be to keep the fluctuations of the foreign exchanges within certain limits so as to promote international trade and investments. It must, however, be noted that national monetary management on the lines discussed above is incompatible with rigid parities of exchange as was the case with the pre-war gold standard. The serious defects in the working of the rigid gold standard as discovered in the post-war period at great cost, on the one hand, and the great success of the experiment of national monetary management during the depression, on the other, make it highly probable that, even if the world returns to a gold standard in the future, it would be a gold standard with rather wide gold points and with parities adjusted from time to time in the light of changing internal conditions in each country.[1]

Gold reserves and their functions.—Now, whether India adopts a modified form of gold standard or not, she will have to keep large gold and foreign exchange reserves for the purpose of meeting international obligations and to smooth out the fluc-

[1] Cf. Keynes, "The Future of the Foreign Exchanges," op. cit.; the *Economist*, October 24, 1936, article on "British Monetary Policy"; and Dey, "World's Currency Dilemma," the *Modern Review*, February, 1937.

tuations of foreign exchanges due to seasonal variations in the flow of import and export trade. This, indeed, was rightly the main objective for which gold and sterling exchange reserves of India were maintained in the past. The size of these reserves must be determined largely with reference to the estimated maximum possible amount of her international debit account. In recent months the gold reserve has been kept steadily at Rs. 44·42 crores at statutory prices and sterling reserves between Rs. 65 and 80 crores at market prices. If the gold reserves are revalued at present market prices, they would go up to about Rs. 75 crores, which together with the sterling reserves, should be sufficient for all normal peace-time requirements. But, over and above this, India should gradually build up an emergency gold reserve as a sort of war chest to meet war-time requirements, and its size should be determined from time to time in the light of various war risks and with reference to the amount of premium which the Legislature is prepared to contribute towards insurance against those risks.

Secondly, since the present-day regulations of the gold reserves in India as in the rest of the world with reference to the amount of the note issue have become thoroughly meaningless on account of the abolition of internal circulation of gold coins, the only regulation that is called for is to lay down the maximum for the note issue from time to time—not, as hitherto, with reference to the gold reserves of the Central Bank either on the proportionality principle or on the fixed fiduciary issue principle, but with reference to the policy of internal economic stability as explained on pages 244–45, together with a small but safe margin for abnormal fluctuations of demand for currency.[1]

Thirdly, since, with the restoration of a flexible form of international gold standard, exchange parities with fairly wide gold points will have to be maintained, it will be necessary for the Government to buy and sell gold bullion and foreign exchange within those gold points without limit. Consequently, there should be only this limited degree of

[1] For the ideas contained on pages 245–46, I am indebted to Keynes, *Treatise on Money*, Vol. II, pp. 273–78.

legal convertibility of internal currency into gold, but at prices fluctuating within gold points, which themselves would be shifting up and down at fairly long intervals in response to changes in internal monetary policies of different countries. But this obligation in respect of convertibility of the internal currency, it should be noted, would not involve any financial liability or any special regulations regarding gold or foreign exchange reserves, because the Reserve Bank would only buy and sell gold at market prices which should include the cost of remittance either way, as was recommended by the Hilton Young Commission.[1] If, over and above this degree of legal convertibility of legal tender token money into gold or foreign exchange, we maintain the present facilities for supplying that form of token money, rupee or notes, which is demanded by the public, we should have fully met all the practical requirements of a good currency system.

Problem of credit control.—But monetary control in a modern community means the regulation of both paper money and bank money (*i.e.*, bank loans leading to the creation of deposits withdrawable by means of cheques). Consequently, it will also be necessary to bring all the commercial banks within the regulative sphere of the Reserve Bank. This has been done with regard to the more important banks, called scheduled banks, which control the bulk of the commercial banking operations of the country. Further, the Indian Companies Act, 1936, Part XA, has provided for a minimum amount of banking regulation with regard to the smaller banking companies, which is calculated to bring them within the control of the scheduled banks and thereby link them up with the Central banking machinery. But a large number of indigenous bankers and money-lenders, who supply a great part of the credit needs of the country, are still without any legal links with the central banking machinery. The necessary degree of integration of the banking structure, however, requires that these latter also should be regulated on lines similar to those that have been adopted with

[1] Vide *Report*, para. 64.

regard to banking companies, namely, minimum capital, registration and licensing, submission of monthly accounts to the Reserve Bank or the Government, and minimum percentage of cash reserves against deposits.[1]

These banking regulations, based on law, should be modifiable from time to time at the discretion of the Reserve Bank, which should be the best judge of whether a particular emergency or an abnormal situation would require a stiffening or relaxation of credit in different parts of the banking system. Thus, for instance, the occurrence of a famine may require that cheap and abundant credit should be supplied to the agriculturists so as to enable them to restart agricultural operations or the outbreak of a panic may call for a lowering of the reserve ratios. Alternatively, again, the sudden outburst of a general speculative mania may need to be curbed by a stiffer control. Besides, since one of the normal instruments of central banking control is an effective Bank Rate, it is necessary that a discount market should be developed by the Reserve Bank on the lines recommended by the Central Banking Enquiry Committee,[2] that the establishment of all the important organs of a modern discount market such as acceptance firms and discount houses and licensed warehouses should be actively encouraged by the Government and the banks, and that the machinery of marketing should be adapted to the requirements of commercial banking.

We shall now conclude by stating that, if India re-orientates her monetary policy and reconstructs the mechanism of her money and credit on the lines discussed in the foregoing paragraphs, it can be expected that she will have made the nearest approach to the attainment of that ideal form of money which modern monetary theory suggests and recent monetary experience indicates.

[1] Also read the *Statutary Report of the Reserve Bank of India on Agricultural Credit*, specially paras. 11, 24, 37–40, and 43–77.

[2] Vide *Report*, Chaps. 20 and 21.

CHAPTER XXVII

THE RUPEE-STERLING RATIO AND THE EXPORTS OF GOLD

By B. R. Shenoy, M.A., M.Sc. (Econ.)

Although India had ceased her habitual net imports of gold and had begun exporting it on balance since June, 1931, these exports suddenly increased in volume and velocity with Great Britain's departure from the gold standard in September, 1931. On occasions, they even exceeded the output of the mines of South Africa. During the seven years preceding April, 1938, their value totalled about Rs. 314·62 crores (37 million fine ounces).

The controversy.—To the world at large, it was a source of some satisfaction that the traditional sink of gold had surrendered an appreciable part of her hoards.[1] Within the country, however, the phenomenon became the subject of a great controversy. On the one hand, the Government emphatically asserted that the free and unrestricted outflow of gold was in the best interests of India. In his budget speech of March, 1932, Sir George Schuster, for instance, observed: ". . . we are absolutely certain that in the present circumstances the best interests of India are being served by allowing free movement of gold to continue. . . ." It is being maintained equally strongly by the public generally, on the other hand, that the exports of gold are in the highest degree injurious to the people and that Government should take measures to prevent the outflow and buy the gold themselves, somewhat in the manner the United

[1] The Controller of Currency has estimated that by April, 1935, approximately 58 per cent of the gold imported since 1920–21 had left the country. Ibid.

States Government did, later, when they abandoned gold. The Federation of the Indian Chambers of Commerce and Industry gave crystallised expression to this view when they resolved on March 26, 1932:—

> "(*a*) The Federation views with grave concern the continuous and heavy exports of gold from India . . . and strongly urges upon the Government of India the desirability of placing an immediate embargo on the export of gold from India, as such a heavy and continuous drain of the precious metal will seriously endanger India's future monetary reconstruction.
>
> (*b*) The Federation further urges on Government the necessity of purchasing gold in the open market at a price fixed on the basis of day-to-day ruling rate. . . ."

So keenly did a section of opinion in the country feel on the subject that, seeing that the Executive was against them and the Legislature beyond their control or powerless to assist them, they drew upon the technique of *Satyagraha* (passive resistance) to prevent the shipping of gold from the country! But with the Police and the economic forces ranged against them, these attempts resulted in little more than traffic congestion.

It is worth while, therefore, making an endeavour to clear the issues involved. But we shall confine ourselves only to the more important among them. First, how were the exports of gold related to the continuance of the rupee-sterling link at 18*d*. sterling a rupee? Second, if the rupee-sterling link had been abandoned, on Great Britain's departure from the gold standard, would the gold and the exchange values of the rupee have been above or below that of 18*d*. sterling? Third, in the light of the answers to these questions, what would have been the best policy to adopt in the interests of the country? While considering these questions, we shall examine the policy actually pursued by the Government.

On the morning of September 21, 1931 (8.30 a.m.),[1] the Government of India received information from the Secretary of State that His Majesty's Government in Great Britain had decided to suspend the gold standard.[2] Perhaps the *communiqué* also contained instructions to take measures for abandoning the standard in India as well. Forthwith, the Governor-General, by Ordinance,[3] suspended (before 10 a.m.)[4] Section 5[5] of the Indian Currency Act, 1927.[6] By order of the Government all banks in India were closed for three days, from September 22 to September 25, 1931.[7] This gave time to the Government to study the situation, to communicate with their principals in London and formulate the details of policy. At the time it was perhaps not clear to them whether it was the rupee or sterling that would have a higher gold value. But the experts of the Government must have fully deliberated upon all aspects of the situation.

Paper Exchange Standard.—The continuance of the rupee-sterling link after the abandonment of gold by sterling amounted to fixing the exchange value of the rupee in terms of the paper currency of a foreign country. That is to say,

[1] Sir George Schuster's speech in the Legislative Assembly on September 21, 1931. *Assembly Debates*, Vol. 14, p. 1089.

[2] *Report of the Controller of Currency*, 1931–32, p. 11.

[3] Ordinance VI, 1931 (*Gazette of India Extraordinary*, September 21, 1931).

[4] Sir George Schuster's speech, loc. cit.

[5] Section 5 of the Act lays down: "For the purpose of determining the equivalent rate applicable to the sale of sterling under this section, twenty-one rupees three annas and ten pies shall be deemed to be the equivalent to such sum in sterling as is required to purchase one tola of fine gold in London at the rate at which the Bank of England is bound by law to give sterling in exchange for gold after deduction therefrom of an amount representing the normal cost per tola of transferring gold bullion in bulk from Bombay to London including interest on its value during transit."

[6] The Gold Standard (Amendment) Act, suspending Subsection 2 of Section 1 of the Gold Standard Act, 1925, which made it obligatory on the part of the Bank of England to sell gold at a fixed rate specified therein, however, could not pass through all its legislative stages until late in the evening that day (about 11 p.m.). Thus, legally, the rupee went off gold even earlier than sterling to keep waiting for the arrival of its master.

[7] The banks in Great Britain were not closed during the crisis. Only the Stock Exchange was closed on September 21, 1931.

it placed the rupee on a Paper Exchange Standard. But, as formerly, the obligation of the currency authority, to buy and to sell sterling unlimitedly at $18\frac{5}{16}d.$ (the upper sterling point) and at $17\frac{49}{64}d.$ (the lower sterling point) a rupee, respectively, continued undisturbed. It, however, now bought and sold paper sterling which fluctuated in gold value, and not, as hitherto, sterling with a fixed gold equivalent. The price of gold in the two countries, not being statutorily fixed, was determined by market conditions like that of any other commodity and reflected the state of currency depreciation. With the movement of sterling unsteady and uncertain, a difference in the gold values of Re. 1 and 18*d.* sterling, therefore, was inevitable. But it was then not clear which of the two would be larger in magnitude.

Under a paper exchange standard, the exchange ratio between the two currencies being fixed, their respective gold values (*i.e.*, the inverse of the price of gold in terms of the two currencies) must tend to move together and, under equilibrium, must conform to the fixed exchange ratio. That is to say, the gold values of 18*d.* and Re. 1 must necessarily keep step with one another and must be identical under equilibrium.

Theoretically, identity of values under equilibrium must hold true, not merely in terms of gold, but also in terms of commodities. In the case of the latter, however, tariffs and other restrictions on their movement, absence of the quality of universal acceptability, comparative satiability of demand and difference in quality, which are inevitable, in some degree, even in the case of standardised goods, give rise to friction and inertia in their price adjustment. And even under equilibrium a comparatively large margin of difference might exist in the values of the two currencies in terms of almost any commodity, other than gold. In their case, a lag of greater or lesser magnitude, depending upon the nature of the commodity, would be present. From this viewpoint it is possible to arrange commodities in the order of their mobility and sensitiveness. Next to gold would come silver

and then the rest of the commodities, standardised goods with a world market taking a high place in the gradation.

But, in respect of the gold values of the two currencies, owing to the universal acceptability of gold and the absence of restrictions generally on its imports, *no such difference can exist* under equilibrium.[1] Any difference will give rise to movements of gold as between the two countries, which will continue until the difference is eliminated and the values are identical, even as the level of water in two interconnected cisterns must necessarily be the same.

Modus Operandi of the Standard.—In the special case we are considering, gold will flow out of India in the event of Re. 1 having a higher gold value than 18*d.* sterling (*i.e.*, if the rupee price of gold was lower than the sterling price, converted into rupees, at the rupee-sterling market rate) or out of Great Britain in the reverse case (*i.e.*, if the sterling price of gold was lower than the rupee price, converted into sterling, at the sterling-rupee market rate). The movement of gold would continue until Re. 1 and 18*d.* sterling were identical in gold value. The *modus operandi* of the equilibrating forces would be somewhat as follows.

In the first case, *i.e.*, in the event of the link undervaluing the rupee, exports of gold from India will give rise to a demand for currency from the Indian currency authority, exchanges would be at the upper sterling point, and until equilibrium will have been reached, exports of gold and expansion of currency would continue. This, combined with the increased demand for gold, will raise the price of gold in India until it corresponded to the sterling price in Great Britain. India would be compelled to buy sterling exchange, which would be offered to her currency authority under provision of the currency law, and thus act as a support to depreciating sterling. Similarly, if the link undervalued sterling, exports of gold from Great Britain would bring about expansion of

[1] Incidentally, it might be observed that, as under it, in the long run, the gold values of the two currencies must necessarily be identical, a paper exchange standard must ultimately lead to a gold standard, so far as the two countries are concerned.

currency, exchanges would be at the lower sterling point and, before reaching equilibrium, sterling will have lost in gold value in its attempts to check depreciation of the rupee.

Assimilation in the gold values of the two currencies would be prolonged if sterling, in the first case, and the rupee, in the other, fluctuated in value or was depreciating. Depreciation would increase the profits of gold exports and would draw out an increasing quantity of gold from the country whose currency got undervalued by the link. The latter would be entirely at the mercy of the overvalued currency and equilibrium would depend upon its return to stability.

For purposes of bringing about equilibrium it is not necessary that gold should be landed in Great Britain on its export from India, or in India, in the reverse case. It may be directed to any other part of the world without prejudice to the process of equilibration. Only, it should be converted into sterling in the first case, and into rupees in the other, either directly (by the sale of gold in Great Britain or India, as the case may be), or *via* a foreign currency (by its sale in a foreign country), and sterling or rupees so obtained should be offered to the currency authority of the gold exporting country in exchange for the latter's currency.

The "gold limits."—In practice, however, a certain difference in the gold values of the two currencies, owing to the expenses incidental to transporting gold and the fluctuation of exchanges between the upper- and the lower-exchange points, might exist without causing any movement of gold. Continuing the example we have considered, it would not become profitable to export gold from Great Britain to India so long as the gold value of a rupee was not lower than that of 18*d.* sterling by more than the gold value of $(x + \frac{15}{64})d.$ sterling, where x represents the expenses, in pence per 18*d.* sterling worth of gold, of transporting gold in bulk from Great Britain to India.

Thus if the gold value of one rupee was a grains of fine

gold and that of 18*d.* sterling, *b* grains, then, in the event of *a* being $>b$, profits of gold exports from India to Great Britain will not appear so long as $(a - b)$ fell short of the gold value of $(x' + \frac{3}{16})d.$ sterling, where x' represents the expenses in pence per rupee worth of gold, of shipping gold from India to Great Britain.[1] And if *b* was $>a$ it would not become profitable to export gold from Great Britain to India while $(b-a)$ was short of the gold value of $(x + \frac{15}{64})d.$ sterling.

The two limits of difference in the magnitudes of *a* and *b*, namely, when $(a-b)$ = the gold value of $(x' + \frac{3}{16})d.$[2] and $(b-a)$ = the gold value of $(x + \frac{15}{64})d.$, would thus mark the limits on reaching which, movements of gold would begin, in the first case out of India and in the second, out of Great Britain. These limits may be termed "gold limits"[3] and should be distinguished from "gold points" under a gold standard and "exchange points" under an exchange standard.

The term "gold limits" refers to the limits of the difference that can exist in the gold values of two currencies linked to one another at a fixed ratio, without

[1] This limit in the difference between *a* and *b* is based upon the statutory upper sterling point of the rupee, namely, 1*s.* $6\frac{3}{16}d.$

[2] See footnote 1, above.

[3] On the analogy of "gold limits," one can speak of "silver limits," which would refer to the limits in the difference in the silver values of the two currencies, which can exist without silver moving out of one country into the other. Similarly, there are "commodity limits" as well. But, for reasons which should now be obvious, "gold limits" would be the narrowest of them all, "silver limits" would probably come next and then would follow "commodity limits." Tariffs, other trade barriers, differences in quality, comparatively lesser degree of elasticity of demand and absence of universal acceptability, each in lesser or larger degree, tend to widen the limits in the case of commodities.

So long as gold and silver are free to move as between two countries on a paper exchange standard, even after equilibrium will have been attained in the commodity values of the two currencies (*i.e.* even after the difference in their values came within the "commodity limits"), if disequilibrium exists in their gold and silver values, inflow or outflow of these two metals will continue and there will take place an expansion of currency issue in the country of the undervalued currency. This will continue even after "silver limits" will have been reached: complete equilibrium will not be reached until the values of the two currencies are within their "gold limits." That is to say, equilibrium in terms of gold necessarily involves equilibrium in terms of all other commodities (under all normal circumstances) and even if equilibrium is attained in terms of the latter, but not in terms of gold, the element of disequilibrium in the situation will remain. Hence the importance of gold in the realisation of complete equilibrium under a paper exchange standard.

gold moving out of them. These are not fixed limits, as the magnitudes of x and x' (which represent the expenses of transporting a grains and b grains of gold, a and b being both fluctuating quantities) are not fixed. Gold limits depend for their magnitude, besides upon expenses incidental to transporting gold, also on the excess or the defect of the upper- and the lower-exchange points, respectively, over the par of exchange.

The gold export limit from Great Britain would be touched when $(b-a)$ = the gold value of $(x + \frac{15}{64})d.$ sterling, and the gold export limit from India would be touched when $(a-b)$ = the gold value of $(x' + \frac{3}{16})d.$ sterling. The Indian gold export limit would also represent the British gold import limit and the British gold export limit would represent the Indian gold import limit.

Symptoms of undervaluation.—The question of whether it was the rupee or sterling that got undervalued by the link would be decided by two symptoms. If, subsequent to the link, gold flowed out of India and continued to do so, it was clear that the rupee was undervalued. For, unless this was so and the difference between the gold values of Re. 1 and 18*d.* sterling was more than that of $(x' + \frac{3}{16})d.$ sterling, *i.e.*, it was greater than the gold export limit from India, exports of gold from the country would yield no profits, and bullion dealers do not get busy for nothing. The second symptom of undervaluation of the rupee would lie in the state of the exchanges. The rupee-sterling exchanges would be above par and at the upper sterling point, or a rate at which the currency authority may decide to buy sterling in exchange for notes. In the absence of the link, the rupee would rise above this limit to reach its economic level, but the link which makes it obligatory on the part of the currency authority to buy sterling in unlimited quantities at the upper exchange point, would prevent it from doing so. Similarly, if gold flowed out of Great Britain, it would be clear that the link undervalued the pound sterling and the rupee-sterling exchanges would be at the lower sterling point, or the rate at which the British currency authority may decide to buy Indian exchange.

Opinion in Great Britain in September, 1931, favoured, as far as possible, resistance to the depreciation of sterling. Practically the whole of her investments abroad, the result of the savings of the nineteenth century, were payable in sterling. By far the larger part of her food supply came from overseas. And her industries had to depend upon imported raw materials. Under the circumstances, a bias towards overvaluation and a corresponding aversion to undervaluation, on the part of the ruling classes and the consuming public generally, is quite natural. It is probable that this factor was largely responsible for the overvaluation of sterling, at such enormous sacrifice, in 1925, when Great Britain returned to gold. The first impulse of the Government, therefore, was to assemble all the available resources to hold in check the depreciation of sterling and to restrain such forces as might accentuate the depreciation.[1]

Ordinance VII, 1931.—Under the circumstances she would not let the rupee be a drag on sterling, which it would be if the link undervalued sterling. Continuance of the rupee-sterling link, under these conditions, would mean a drain of gold from Great Britain, further inflation and further depreciation of sterling. Sterling would be at the mercy of the rupee and those who controlled the fate of the rupee would control the fate of sterling also. But the reverse situation, namely, the rupee providing a support to sterling, which it would do if the link undervalued the rupee, was altogether welcome. Gold

[1] A British official statement issued on the evening of September 20, which announced the decision of the Government to suspend the gold standard, observed: ". . . They (the Cabinet) desire to repeat emphatically the warning given by the Chancellor of the Exchequer that any British citizen who increases the strain on the exchanges by purchasing foreign securities himself or assisting others to do so is deliberately adding to the country's difficulties. The banks have undertaken to co-operate in restricting purchases by British citizens, except those required for the actual needs of trade or for meeting existing contracts, and should further measures prove to be advisable, His Majesty's Government will not hesitate to take them. . . ."

It would appear that this warning had not the desired effect. For, on September 22, the Treasury by virtue of the powers conferred upon it by the Gold Standard (Amendment) Act, 1931, prohibited purchases of foreign exchanges or transfer of funds, by British subjects or persons resident in the U.K., except for financing: (1) normal trading requirements; (2) contracts existing before September 21, 1931; (3) reasonable travelling or other personal purposes. But the sale of exchange to finance the imports of gold into the country, unlike in India, was not prohibited.

would then flow out of India and the currency authority would be forced to buy sterling and thus help in arresting its depreciation. The measures to be adopted by the Government of India must therefore be such, or so must have argued the experts of the Government, that should it turn out that the link undervalued sterling, sterling must be free to abandon the rupee to its own fate, whilst, in the second case, the rupee must not leave sterling behind and the link must then be continued. These requirements of the situation were adequately met by the Ordinance[1] published on the evening of September 24, 1931, *i.e.*, the evening previous to the reopening of the banks after the three days' holiday.

This Ordinance restricted the sale of sterling by the Government. It laid down that sterling could be bought for the following purposes only:—

(1) Normal trade requirements, but *not for the import of gold or silver coin or bullion*. . . . ;

(2) for contracts completed before September 21, 1931; and

(3) for reasonable personal and domestic purposes.

Certain rules were framed under the Ordinance which empowered a Managing Governor of the Imperial Bank to call upon any recognised bank[2] to satisfy him that it had not been selling foreign exchange for any purpose other than those specified in the rules and that it had sold all its purchases of foreign exchange before asking for more. He could also suspend for seven days the recognition of a bank for not satisfying him in these respects pending action by the Government.[3]

The provisions of the Ordinance enabled the Government to sit on the fence. In the light of the course of events as they revealed themselves, they could then jump on

[1] Ordinance VII, 1931, *Gazette of India Extraordinary*, September 24, 1931.

[2] The Ordinance gave names of 24 Exchange Banks as recognised banks, which included the Central Bank of India and the Bank of Baroda.

[3] Ordinance, loc. cit.

what side served their interests best. Since it imposed restrictions on the sale of sterling, the Ordinance ensured that, if the link undervalued sterling, the link could be snapped and the rupee could thereby be prevented from eking out a living at the expense of sterling. For, under it, sterling would not be available to pay for the imports of gold—exchange would now be at the lower sterling point and the exchange market would depend upon the currency authority for the supply of its excess exchange requirements—and the equilibrating forces through the agency of gold would not operate as a consequence. But the market may yet turn to silver, which is only next to gold in point of mobility and sensitiveness, and the imports of silver into India may cause the depreciation of sterling to the level of the rupee. The Ordinance, therefore, laid down that sterling would not be made available for the finance of silver imports also. With gold and silver not free to come into the country, the forces of equilibration through the agency of these two metals would not function. The gap between the values of these two currencies, therefore, would first reach the "gold export limit" from Great Britain ("gold import limit" into India) then the "silver export limit" (the "silver import limit" into India) without gold or silver being imported into India, and would then exceed these two limits.[1] That is to say, the market rate of exchange, already at the lower sterling point, would fall below it in search of its economic level.

There will thus result a disparity between the market rate of exchange and the official rate. By the extent of the margin between the two, the currency authority would be suffering losses every time it sold sterling exchange for rupees. And sooner or later, the currency authority would be compelled to abandon the link of the rupee to sterling or, as it would be more appropriate to say, give up the show of maintaining the link. For the link can be said to have snapped when the market rate of exchange persisted below the lower sterling point.

But should the rupee have a higher gold value than sterling, the Ordinance would not prevent sterling from

[1] See footnote 3, p. 255.

being saddled on the rupee. It left unrestricted the outflow of gold, which must now take place under the stimulus of profits that the undervaluation of the rupee would yield. Sterling acquired by the sale of this gold abroad would be offered to the currency authority in India in exchange for rupees. Sterling would be withdrawn from the market and rupees released into it. In the process India would be supporting the British currency and depreciating her own.

Actually, however, the latter of the two alternatives came out true, *i.e.*, the rupee got undervalued by the link. But the restrictive clause for the sale of sterling in the Ordinance, probably, misled the market at first and may have been responsible for the demand for sterling on September 25, when the banks reopened after the three days' enforced holiday. But it soon discovered that to demand sterling from the currency authority was a false step and that it could make a profit by offering sterling to it instead, acquired by the sale of gold abroad. The demand for sterling accordingly ceased on September 26,[1] exchanges steadily rose, and by the end of October, sterling quotations reached 1*s.* $6\frac{1}{32}$*d.* Tenders for £500,000 were invited by the Government at this point and allotted at 1*s.* $6\frac{3}{32}$*d.* The weekly offer was raised by successive stages to £1 million and almost until April, 1937, there was hardly any week in which Government was not able to obtain the full amount offered and effect besides purchases of "intermediates"[2] at $\frac{1}{32}$*d.* above the tender rate.[3]

The phenomenal exports of gold and the state of the exchanges were symptomatic of the undervaluation of the rupee. Barring short intervals[4] the exchange value of the

[1] *Report of the Controller of Currency*, 1931–32, p. 12.

[2] The term "intermediates" refers to the purchases of sterling by the Government during the week, except on tender days, *i.e.*, the days when weekly tenders for sterling are offered by the Government.

[3] *Report of the Controller of Currency*, 1931–32, p. 12.

[4] If from the middle of October to the middle of November the rupee was weak it was due to certain temporary disturbing factors which led to speculation for a fall. The widespread campaign by the Currency League for the devaluation of the rupee below 16*d.*, coincided with the discussions on the Reserve Bank Bill in the Legislative Assembly and speculators had probably entertained the hope that by amendments to

rupee for practically the whole period following September, 1931, was above par and at or near the upper sterling point. "Intermediates" were sold most of the period at $\frac{1}{32}d.$ above the weekly tender rates, even when these were 1*s.* $6\frac{1}{2}d.$ On such occasions, sterling exchange could be said to have remained at 1*s.* $6\frac{5}{32}d.$ When it was established beyond doubt that sterling was firmly saddled on the rupee, restrictions on the sale of sterling exchange were removed on January 30, 1932, by notification in the *Gazette of India*.[1]

Government's defence of its policy.—The experts and spokesmen of the Government, however, were never wanting in their attempts to defend the Government's policy and to make out a case to show that in its formulation they were solely guided by Indian interests. Perhaps the ablest defence was the one put forth by Sir George Schuster. The Finance Member, in his budget speeches of 1932 and 1933, made out certain, what at first sight appear to be very relevant and sound points, besides certain others not exactly of that order.[2]

He argued that during the past 30 years India, on balance, had hoarded Rs. 700 crores worth of gold and that the amount exported was only a fraction thereof; that it would

the Bill there was a chance of devaluing the rupee. They had, therefore, made extensive forward purchases of exchange. The banks were thus unwilling sellers except at low rates and exchange fell gradually to 1*s.* $5\frac{13}{16}d.$ This situation, however, righted itself immediately the Government made it clear that they were not willing to accept amendments to the Bill which would alter the ratio. By December 28, exchange was firm again and above par.

[1] *Report of the Controller of Currency*, 1931–32, p. 12.

[2] In defence of the unrestricted outflow of gold, he cited, for instance, the examples of Belgium, France, Holland, and the U.S.A., which had then put no such restrictions. (Budget speech, op. cit.)

But, of course, Sir George Schuster did well know that these countries being then on the gold standard, consistently with their remaining on gold, could not afford to impose these restrictions. To have cited their examples in support of not restricting exports of gold from India, a country off the gold standard, perhaps only illustrated the Finance Member's anxiety somehow to produce arguments in support of his policy. But in putting it forth before the Legislative Assembly he was probably aware, as the late Sir Basil P. Blackett before him was aware, on similar occasions, of the vastness and depth of the knowledge of Economics on the part of our Legislators!

be unfair to interfere with the liberty of the sellers in disposing of their gold abroad to tide over the present crisis; that it was only proper to draw upon the accumulated reserves in times of difficulties; that the future of gold was uncertain and that it was therefore best that India disposed of it now; that a part of the proceeds at least of the gold had been invested; and so on.

All this might indeed be true, but it could be no justification for disposing of gold at a loss, nor for sending out of the country the fruits of gold appreciation, which could have been made use of to relieve the burden on the tax-payer. The objection was not against gold going out of the country; nor against the hard-hit sellers of it drawing upon their reserve strength; much less against the proceeds being invested; but against a policy which involved losses on double account, in respect of gold exports; which landed us in instability in the name of stability; which enforced upon the country an altogether unplanned and erratic inflation and currency depreciation, on the absurd basis of the difference between the gold values of two unstable currencies, wholly unrelated to what the requirements of the body-economic may be; and in the bargain dumped upon the country a mass of progressively depreciating sterling paper in exchange for a progressively appreciating commodity, gold. If a certain other policy, while promising to ensure all the advantages mentioned by Sir George Schuster and many more besides, would ensure in addition the avoidance of its evils as well, that policy was worth at least a moment's consideration.

But probably the strongest point of Sir George Schuster was that the exports of gold had improved India's credit in the world market; that they had enabled remittances on account of Home Charges to be made without having had to borrow; that they had enabled the repayment of sterling debts which had matured on January 1, 1932, of the value of £15 million, and that they had strengthened the currency reserves of the Government.

In support of this conclusion the Finance Member formu-

lated a balance-sheet of gold exports and the disbursement of its sale proceeds for a period of 15 months from September, 1931, to December, 1932. To quote his own words:

"In this period of fifteen months, India on balance exported 107·08 crores of gold. We may thus take it that private individuals during this period acquired out of the proceeds of gold exports balances in external currency, probably mainly in sterling, to the extent of £80⅓ millions. During this same period exports of merchandise were 187·37 crores and imports 161·45 crores, giving a favourable balance of 19·92 crores, equivalent to, say, £15 millions. This sum also may be taken as having been converted into external currency balances by private individuals. Adding these £15 millions acquired against merchandise to the total of £80⅓ millions acquired through gold exports, the total external balances acquired by private individuals from October 1, 1931, to December 31, 1932, amounts to £95⅓ millions. Out of this sum Government has acquired by its purchases in the market as currency authority not less than £69⅔ millions.

"In the first place Government has used about £34 millions in meeting its ordinary recurrent commitments.

"Secondly, it has used £15 millions in discharging the 5½ per cent sterling loan which matured on January 1, 1932, thereby liquidating an obligation which cost it £825,000 equivalent to Rs. 110 lakhs per annum, and greatly strengthening its credit in London.

"Thirdly, Government has added about £11 millions to its currency reserves, and lastly, the balance of £9¼ millions was added to the Government's Treasury balances, and is really potentially available for further strengthening of its currency reserves.

"Government therefore made good use of the abnormally high amount of sterling which it was able during these 15 months to purchase as a result of the gold exports."

The defence examined.—This is an account of how during a period of 15 months slightly over 14 million ounces of gold

valued at Rs. 107·08 crores left the country and how Sir George Schuster got in exchange for it a mass of progressively depreciating commodity, sterling paper, and what use he made of that paper. But it was no more a justification for depriving the country of profits of gold appreciation and for landing us in instability, than the first series of arguments advanced by him.

It may be worth while, therefore, to picture to ourselves what the situation would have been like if, on prohibiting the exports of gold, Sir George Schuster had bought the gold. The total purchases of the Government for the period of 15 months would then have been 14 million ounces of fine gold, supposing the same amount of gold would have been offered for sale. Of this about 2·6 million ounces would have been required to repay the debts falling due on January 1, 1932 (£15 millions).[1] On September 21, 1931, there was in the Government reserves £16 million sterling. These could have been passed on to Great Britain as part of the Home Remittances. The balance of £18 millions of the Remittances would have required about 2·9 million ounces of gold. The remaining gold could have been put in the Government's reserves and balances, in part replacing the sterling securities in them.

Thus our external liabilities could have been met in lesser gold than we have had to part with actually. Gold in the reserves would have inspired far greater confidence than sterling, both internally and externally, and what is more, it would have enabled stabilisation of our currency independently of Great Britain and with less embarrassment to ourselves. Also, profits of appreciation of gold in the reserves would have accrued to the Government.

The rise in the rupee price of gold from a parity rate of Rs. 21-3-10 when the rupee was on gold to over Rs. 30 subsequent to the departure from the gold standard by India, has invoked the argument that the sellers of gold have made profits out of the transaction. Besides the Finance Member one or two Indian Economists have

[1] This calculation has been made on the basis of the price of gold on January 1, 1932, which was £5 17*s*. 11*d*.

subscribed to this theory.[1] It is worth while, therefore, paying some attention to it.

It should be easy to appreciate, however, that these profits were wholly illusory. They were similar to the profits that anyone can realise, or feel that he has realised, by measuring six yards into a piece of cloth only three yards long when bought from the *bazar*, by cutting down the length of the yard-stick to one half. The larger number of rupees were now each of lesser value and the rise in the price of gold only indicated the depreciation of the rupee.

Indeed far from making profits, sellers of gold would be losers from a double view-point. Consistently with the (fixed) exchange value of the rupee, the rupee price of gold will not have risen sufficiently high during the time exports of gold take place. That is to say, the sellers of gold, even as they parted with it, would be getting fewer rupees than they should: at the existing sterling equivalent of the rupee the equilibrium price of gold would be higher than was paid to them.[2] This loss would be wholly owing to the undervaluation of the rupee incidental to its being linked to sterling. It could be avoided only by breaking the link. Also, ignoring temporary downward movements, the price of gold since September, 1931, had been steadily rising. It rose from a par rate of Rs. 21-3-10 to over Rs. 30 per tola. This appreciation in the price of gold escaped the hands of those who parted with gold during the period of its appreciation.

The "profit" illusion.—Confusion of thought has also been responsible for the argument that the sellers of gold have gained, not only in terms of rupees but also in terms of commodities. An attempt has been made to evaluate this gain in "goods value."[3] The index numbers of France and Holland

[1] "A Review of Gold Export Fallacies," by B. P. Adarkar, *Indian Journal of Economics*, January, 1936, Vol. XVI, p. 307.

[2] This proposition I have worked out algebraically elsewhere. See my article entitled, "Exports of Gold from India: an Analysis of the Government's Currency Policy," *Indian Journal of Economics*, July, 1936, Vol. XVI, p. 11, footnote 11.

[3] "A Review of Gold Export Fallacies," by B. P. Adarkar, *Indian Journal of Economics*, January, 1936, Vol. XVI, Part III, p. 307.

(countries which remained on the gold standard) for 1931 and 1934 have been made use of to estimate what the Calcutta index numbers would have been like in 1934 if the rupee had continued on gold. These estimates have given rise to the conclusion that at the ruling prices of gold, a tola of gold in 1934 actually bought to the sellers anything between a maximum of 37·3 and a minimum of 32·0 units of goods. But if the rupee had continued on gold, so goes the argument, the goods value of a tola of gold would have been only 26·4 units, at the maximum. That is to say, those who parted with their gold gained in commodities to the extent of anything between 5·6 units and 10·9 units.

This arithmetic of index numbers ignores the fundamental absurdity of the performance. For it attempts to prove that to-day (1934) 180 grains (one tola) of gold, *when the monetary unit of the country is off the gold standard*, would buy in the market *more of* commodities than what *the same amount of gold* would buy *also to-day* (1934), *if the monetary unit had continued on gold* instead of abandoning it! Whether a country is or is not on the gold standard, and whatever the nature of that standard, 180 *grains of gold* (*as* 180 *grains of copper or tin*) *must buy one and the same number of "units" of commodities at any one given time and place.* Since the continuance on the gold standard by India would involve a greater demand for gold, perhaps it is possible to argue that a tola of gold would buy *more of* commodities when the rupee was on gold than when the rupee was off it. In no case could it buy *less*. Any attempt to prove to the contrary must necessarily be nonsensical, and to use index numbers in doing so would be to miss their purpose and significance.

The exports of gold have influenced the currency situation in the country. They have led to an excess issue of currency, both in coins and notes. In this respect the year 1931–32 divides itself into two parts: the period up to the end of September, 1931, and the rest of the year. During the first period currency was being returned to the Government at a rate commensurate with and even exceeding that of the

previous two years. But during the latter period both notes and coins came to be absorbed on a scale which varied with the volume[1] of gold exports. For the year 1931–32 the net absorption of currency was Rs. 21·4 crores. During the previous two years, on the contrary, on balance the country had returned to the currency authority Rs. 40·5 crores and Rs. 33·0 crores worth of currency, respectively. In 1933–34 again the net absorption of currency was Rs. 13·2 crores. In effect this amounted to an expansion of currency which was commensurate with the rupee value of gold exports.

Three main alternatives of policy.—When Great Britain suspended the gold standard, the Government of India had before them three main alternatives of policy: (1) to continue the link of the rupee to sterling at the existing ratio or a different one; (2) to abandon the link and allow the rupee to find its own level; and (3) to link the rupee to gold at a convenient parity.

In view of the inadequate stock of gold in the reserves[2] the last of these alternatives was not practical finance, at any rate immediately. Also, it would have been extremely difficult to make the right choice of gold parity for the rupee when the currencies of the larger part of the world were on the defensive and one could not be too certain of their continuing on gold for long. At all events the fixing of the gold value of a currency unity was too complicated a problem to be decided upon in a moment of excitement and hurry. Of the other two alternatives the Government selected the first, with what injury to the interests of the country we have seen above.

[1] In this connection the following remarks of the Controller of Currency are of interest: ". . . The year was divided into two clearly marked periods, the first up to the end of September when as a result of falling prices the return of currency continued on a scale commensurate with, and even exceeding, that of the previous two years. During this time currency was contracted to the extent of 26,87 lakhs. In the latter half of the year with the abandonment of the gold standard prices showed a tendency to rise and the finance of India's gold exports necessitated currency expansion on a large scale. . . ." *Report*, 1931–32, p. 16.

[2] On September 5, 1931, there was in the reserves Rs. 7·2 crores' worth of gold against a note circulation of Rs. 148·5 crores, or a gold reserve of about 5 per cent.

The third course of abandoning the link and pursuing an independent policy was left alone. But this combined with an embargo on the exports of gold and the buying up of gold by the Government would have served best India's interests. This would have given us freedom of monetary policy and we could then decide upon either further inflation and depreciation before stabilising the currency or stabilisation without further depreciation. If we were to discover that our salvation lay in depreciating the rupee to the level of sterling, remaining below it or somewhat higher, our hands being untied we could act accordingly. From the state of the exchanges and the movement of gold we could have realised almost at once that the market value of the rupee was higher than that of 18*d*. sterling. That would have banished the apprehension of Sir George Schuster that the burden of the Home Charges would be heavier if the rupee fell below sterling. Actually, by undervaluing the rupee, we had to pay a larger number of rupees to meet the Home Charges than we need have if the rupee-sterling link had been abandoned.

After delinking, possibly we might have decided upon a certain measure of depreciation since the larger part of the world had taken to this course, and also to atone for the double sin of first overvaluing the rupee and then linking it to an overvalued sterling, in 1927. The buying of gold by the Government would have been a convenient method of currency expansion. It would have enabled them to control the volume and the pace of the expansion, unlike under the régime of the rupee-sterling link. The link rendered any attempt at controlling currency expansion impossible. By preventing an adjustment of the exchanges to within their gold limits, they would merely succeed in stimulating the exports of gold and further upsetting any tendency towards equilibrium. But the expansion of currency caused by the buying up of gold could be successfully neutralised, if required, by the sale of securities, the issue of a loan at home, or by curtailing the normal outflow of money into circulation from the currency authority.

The profits of gold appreciation would then have accrued

to the Indian Treasury. Our foreign liabilities as they fell due could have been met by selling the accumulated gold, in the world market. As shown above,[1] in this manner we could have discharged our sterling obligations in lesser amount of gold than we have had to part with actually. A part of the gold would have been needed for currency stabilisation, when the time for this arrived. Having realised at such enormous cost the dangers of a sterling exchange standard, we could have seized hold of this opportunity to place the rupee on a gold bullion standard.

The buying up of gold by the Government would have involved no risk. Once the Government made up its mind at what level to fix the price of gold statutorily, there was no risk whatever in buying gold at prices lower than this: the Government would gain by the difference between the two prices. Actually, in place of these profits, the Government's policy landed them into losses measured by the extent of the depreciation of sterling which they got in exchange for the gold exported from the country.[2]

Delinking harmful to British interests.—But it must be admitted at once that this policy would have provided no relief to sterling. With the support of the rupee removed, its low-level mark would have been far lower than $3·15 to which it had reached in November, 1932. If the Government were to attempt to prevent this fall, the cost would have been enormous, even supposing foreign credits were available for the purpose.[3] The Exchange Equalisation Fund, under the circumstances, would have been filled and emptied several times over.

To ask for abandoning the rupee-sterling link or for an embargo on the exports of gold (this would have snapped

[1] See p. 268.

[2] Sterling has depreciated by about 40 per cent since its departure from gold.

[3] It may be noted that the British Government before abandoning the gold standard had asked for further credits from the Governments of United States of America and France on September 18, 1931, but without success.

See the speech of the late Viscount Snowden (then Mr. Philip Snowden) in the House of Commons on September 21, 1931. *Hansard*, Vol. 256 of 1931, p. 1294.

the link) was therefore asking for far too much. It was to pitch our ambition too high.

To summarise our conclusions. On Great Britain's departure from the gold standard, the Government of India, no doubt under instructions from their principals in London, sat on the fence until the trend of events was clearly revealed. While they announced the continuance of the rupee-sterling link, they imposed restrictions on the sale of sterling generally and in effect prohibited the imports of gold or silver into the country (by prohibiting the purchase of sterling for the finance of these imports). If the link had undervalued sterling, they could have prevented the rupee from being a drag on sterling, first by tightening the restrictions on the sale of sterling and then by stopping the sale altogether (to which the restrictions must necessarily lead) This would abandon the rupee to its own fate and sterling would be free to follow an independent course, unhampered. But as the exports of gold from the country were left free, the rupee had no choice but to shoulder the burden of sterling, if the link undervalued the rupee.

The second of the two alternatives having come true, Government jumped down from the fence on the side of the rupee-world sterling link. It provided the much-needed support to double, and drew out gold from the Indian hoards which it to an Great Britain to meet her gold obligations and the G thened her credit. But to India this policy meant cu threefold consequences of exports of gold, expansion of currency, and depreciation without plan.

In respect of gold exports she suffered losses on double account. The sellers of gold got fewer rupees than the fixed exchange value of the rupee should entitle them to, and the appreciation in the value of gold slipped out of their hands. Also, in place of gold (an appreciating commodity) gone out of the country India got in exchange steadily depreciating sterling paper. Exports of gold brought with it expansion of currency to finance these exports. This caused depreciation of the rupee. But the expansion and depreciation were wholly unrelated to what the econmic circumstances of the country might demand.

They depended upon the margin of the difference in the gold values of sterling and the rupee. They were the result, not of any well executed policy, but the consequence of sterling dragging behind it the rupee, in the course of its depreciation. They were wholly erratic and unplanned.

The continuance of the link with sterling necessarily involved surrender of all monetary autonomy. The rupee was at the mercy of sterling and the fate of the rupee would be decided by those who controlled the fate of sterling. In respect of the time and parity for stabilisation the country could have no initiative whatever.

In view of the inadequate supply of gold in the reserves and the state of general monetary uncertainty prevalent at the time, it was neither practicable nor desirable to link the rupee directly to gold. But there can be little doubt that the best policy which the Government could have pursued with profit to themselves and advantage to the community was to delink the rupee, let it discover its own value, impose an embargo on the exports of gold, and buy the gold. Thus released from all shackles, India could have watched the situation as it developed and formulated her policy accordingly. We could then keep the rupee on a par with sterling, above or below it, just as we liked. To depreciate the rupee to the level of sterling, if therein lay our salvation, it was not necessary to chain the rupee to sterling. Under the link the depreciation was brought about by the currency authority buying sterling. The same result could be attained by buying gold or domestic securities.

What U.S.A. did under similar circumstances.—This was what most countries who were masters of their own monetary policy had done when they abandoned the gold standard. The U.S.A., for instance, when it went off the gold standard in 1933 imposed an embargo on the exports of gold and the Treasury bought all the available gold. The buying up of gold by the Government caused currency expansion and depreciation of the dollar. And when the dollar reached the level at which it was thought

proper to stabilise, restrictions on the sale of gold were lifted and the Treasury expressed its willingness to sell the gold. Since most of the gold bought prior to stabilisation was at prices lower than 35 dollars the transaction yielded to the U.S. Government considerable revenues by way of profits which were used for reducing the national debt. In March, 1934, Mr. Morgenthau, Secretary of the U.S. Treasury, applied no less than 675 million dollars (about £138 million) of the profits to pay off 600 million dollars' worth of Consols and 75 million dollars' worth of Panama Canal Bonds.

Similar profits which India could have earned, if the Government had followed the same policy, actually were split. But it would have provided no relief whatever to sterling. Sterling under the circumstances would have fallen much lower than it did actually, to prevent which would have meant enormous cost. It was not possible, therefore, that the experts of the Government would advise them to sever the link of the rupee with sterling.

CHAPTER XXVIII

DEVALUATION OF THE RUPEE

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DEVALUATION AS A WIDER ISSUE

We must emphasise almost at the very outset that devaluation as an immediate economic issue has wider bearings and must be visualised in a broader perspective. Clear and rational thinking on this issue is impossible unless we look upon this problem in the wider perspective of currency stabilisation sought to be achieved in India during the post-war period.[1] The present controversy has its roots in the past. There is a general feeling that the Government of India sowed the wind before the depression began and the country has been reaping the whirlwind since then. It is argued that the rupee had been internally overvalued in 1926 (according to some much earlier) and since then the Indian economic life had to pass through a process of devastating deflation which initiated the economic depression in 1929, or at least the effects of which were superimposed upon the effects of the world economic depression. Hence the demand for devaluation is nothing but a modest demand for correcting the internal overvaluation of the rupee, a persistent cause of economic disequilibrium. On the other hand, the currency authorities hold that since the rupee had already been stabilised in 1926 after careful revaluation the present ratio should be respected as a basic norm which should not be disturbed by "monkeying with the ratio." A controversy like this cannot be properly understood unless we examine the rationale of the post-war stabilisation of the rupee.

There is a general consensus of opinion amongst economists on what constitutes the *sine qua non* of monetary

[1] Vide the writer's *Whither Rupee?* for a full discussion.

stabilisation. It is generally agreed that the value of the currency unit of a country should be such as to maintain equilibrium not only in the internal economic structure but also in the balance of its international transactions. The criterion for international equilibrium (from which a country depending largely upon its foreign trade for solvency should not depart) is the "absence of persistent gold movements and of abnormal capital movements motivated by an anticipation of a fall or rise in the exchange rate."[1] An important dynamic factor which tends to upset the balance of international transactions in relation to a certain country is a fundamental change in the barter terms of trade which affects the external value of a country's currency. If such a change is not somehow counteracted, or if the so-called normal parity of exchange is not adjusted to the altered terms of trade, an artificial pegging of exchange at a particular level becomes disastrous in its effects on internal as well as external economic equilibrium. From the point of view of the internal economic structure stabilisation involves a balance between the cost and debt structure and prices and between export prices and other prices.

A point which is very often missed by those who take part in the ratio controversy is that under a system of pegged exchange no parity of exchange should be regarded as representing a so-called "natural" level or norm which is sacrosanct. Any student of the history of Indian currency knows that the pre-war exchange rate of 1*s.* 4*d.* to the rupee was entirely the product of accidental circumstances when it first established itself and was thereafter deliberately maintained at that level by currency management. The present ratio is in a sense as artificial as the ratio of 1*s.* 4*d.*, since it has been and has to be maintained by artificial means under a system of exchange standard. Hence it is irrational to be sticklers for any particular ratio under the delusion that somehow it represents a norm. Any ratio which is conducive to and consistent with comparative economic stability under particular circumstances should be the objective of monetary

[1] Haberler, *Prosperity and Depression*, p. 334.

policy. In any case what the norm is should be an open question, for exchange stability must needs be a means to economic stability as defined above and not an end in itself which may be pursued irrespective of the fundamental maladjustments of our economic life in recent years. During the present economic depression most of the cherished norms of political and economic life have radically changed owing to revolutionary maladjustments in political and economic life.[1] If, therefore, Indians ask the Government of India to review the question of the rupee ratio and decide what the norm should be in the present circumstances they should not be accused of the childish desire of "monkeying with the ratio," specially when Indians know to their cost that all these years it is the rupee which has been playing strange monkey tricks with them.

POST-WAR CURRENCY STABILIZATION

In reviewing the rationale of post-war currency stabilisation attempted in India at the very outset one is irresistibly reminded of the Government of India's misadventure (we refrain from calling it "monkeying") with the rupee ratio in 1920. We must mention in this connection what Professor Fisher has aptly called the "disastrous deflation" of 1920 in United States of America which the Federal Reserve authorities tried to explain away as a phenomenon caused by non-monetary factors. The deliberate deflation in America led to deflation in other countries which were anxious to prevent the depreciation of their currencies in terms of dollar. In this way a general process of deflationary contraction was initiated in March, 1920, after the short-lived post-war boom. In India the currency authorities had blundered into overvaluing the rupee at 2*s.* (gold). The rate had eventually to be abandoned, because internal prices could not be made to fall to the same extent as external prices. But in the heroic effort to maintain the new "norm" they had resorted to disastrous

[1] For example, "free trade" and "gold standard" which were so long almost the unalterable norms of British economic life have recently ceased to be so!

deflation, which continued till Indian exchange was left to find its own level and moved in sympathy with the steadily falling internal and external prices.[1] The result of heavy price deflation was that industrial development, which had started in India during the war and was well under way during the post-war boom, received a setback. Particularly the protective effects of the raising of the general tariff from 7½ to 11 per cent in March, 1921, and to 15 per cent in March, 1922, and of the raising of the tariff on luxury goods from 20 per cent to 30 per cent, were obscured by the general effects of the trade depression caused by world-wide deflation. But it must be said to the credit of the currency authorities that by allowing the exchange rate to find its own level they protected the internal economic structure to a certain extent against the fluctuations in gold prices during the boom of 1919 and 1920 and the slump of 1921 and 1922. From 1922–23 onwards the parity of the relative levels of internal prices in India, and in countries which were the best customers of India, created an impression that Indian exchange was moving to a position of stability. In 1922–23 the price levels in the United Kingdom and India remained remarkably constant. In Japan also the price level was well maintained. But in America it registered a slight rise. Between 1923–24 and 1925–26 the wholesale prices in U.S.A., Japan and United Kingdom continued to be relatively stable. In 1925–26 the comparative values of Indian exports and imports also were almost back to their pre-war relationship. Exchange was also stable at 1*s.* 6*d.* throughout the year. And the picture of stability in the eyes of the currency authorities was completed by the price indices in India, America and United Kingdom converging towards the same level. Eventually, the rupee exchange was stabilised at 1*s.* 6*d.* in 1927.

THE 1S. 6D. RATIO

But did the pegging of exchange at 1*s.* 6*d.* really give us stabilised money? Were the simple criteria of economic

[1] The process of artificial contraction of currency continued up to August, 1923.

equilibrium carefully applied to the existing situation? In the first place, the stability of the exchange-rate throughout 1925–26 was not necessarily a sign of economic stability. Under an exchange standard it was easy to bolster up the exchange rate and maintain it at a certain level by currency manipulation. The grinding process of deflation which had started much earlier made this task easier, and since the middle of 1924 the pace of further deflation was set by England. What happened was that in England currency authorities had recourse to active deflation for going back to the pre-war gold parity. In June, 1924, the pound sterling was about 12 per cent below the pre-war gold parity. As the result of deflation the sterling price index fell by about 9 per cent between June, 1924, and February, 1926. We observe a similar phenomenon of drastic deflation in India where also the wholesale price index fell by 11 per cent during the same period and the rupee-sterling exchange rose from 1*s.* 4*d.* to 1*s.* 6*d.*, registering a rise of 12½ per cent. Secondly, comparative stability of the internal price level is nowadays no longer regarded as the only adequate criterion of economic stability. In U.S.A. just before the financial crisis which led to the Great Depression the index of wholesale prices was remarkably steady, but the steadiness of the index masked the inherent economic disequilibrium which subsequently caused a world-wide depression. The price level alone is never an adequate guide for the determination of the policy regulating the currency and credit of a country. Speaking of credit policy, Governor Strong, of the New York Federal Reserve Bank, one of the greatest bankers that America has produced, said, "Just as credit is one of the influences upon the price level, so the price level should be one of the influences in guiding a credit policy," and he suggested a few considerations which a Central Bank must have in view in determining a particular policy: "Is labour fully employed? Are stocks of goods increasing or decreasing? Is production to the country's capacity? Are transportation facilities fully taxed? Is speculation creeping into the productive and distributive processes? Are orders and repeat orders being booked much ahead?

Are bills being promptly paid? Are people spending wastefully? Is credit expanding? Are market rates above or below Reserve Bank rates?"[1] As a matter of fact in Sweden the Riksbank consults not only the wholesale price index but also the basic consumption index (cost of living index) and other available indices such as those of production, trade and employment. Did the currency authorities in this country give sufficient weight to considerations such as these before they decided upon the revaluation of the rupee? Were they sure that internal prices which were suddenly deflated after the currency débâcle of 1920 had been adjusted to wages and other money incomes, to debts and fixed charges of the agriculturists and to the various other elements of cost of production which cannot be quickly readjusted? Did they take into account the obvious fact that owing to the vast size of the country and the absence of sufficient economic mobility the costs-prices equilibrium ought to take a much longer time to be completed in India than in other industrial countries? Did they make allowance for the necessary time lag? Thirdly, the mere fact that the indices of wholesale prices in United Kingdom, America and India had converged to the same level (160) did not deserve the significance which was attached to it. Since the dynamics of the price movements in these three countries were not the same, the price indices reaching a particular figure in the course of varying fluctuations did not really mean that conditions were necessarily favourable to international equilibrium, or that Indian prices had been brought into harmony with the national price levels of countries which were the most important customers of India. In fact subsequent tendencies provide the clearest refutation of such confused reasoning. Between 1924 and 1929 the British Board of Trade index registered a fall of over 17 per cent and the Calcutta index similarly showed a fall of over 18 per cent. Such a parallel movement is explained by the common policy of deflation consequent on the overvaluation of sterling in relation to gold since 1925. But in

[1] Interpretations of Federal Reserve Policy in the speeches and writings of Benjamin Strong, New York, 1930, p. 233.

U.S.A. the index of the Bureau of Trade Statistics fell by only 3 per cent, while the index number of wholesale prices both in Germany and France remained steady during the same period. The fact is that the general movement for international monetary stabilisation in 1924 had an unsound basis. As Sir Walter Layton said in 1933, "The mistake that we made in 1924 was to endeavour to set up an international monetary system without first making sure that the economic background was right." Moreover it is necessary to emphasise in this connection that "measurements of purchasing-power parity based on comparisons of price levels or of changes in price levels in two countries afford only very rough and unreliable criteria of overvaluation or undervaluation of a country's currency."[1]

CHANGE IN THE BARTER TERMS OF TRADE

A most important dynamic factor which has threatened the equilibrium of India's balance of international payments in recent years, but which has been ignored by the authorities responsible for post-war monetary stabilisation in India, is the fundamental change in the barter terms of trade. In official statistical publications the index numbers of external prices of imports and exports respectively in the case of different countries are available for a series of post-war years. If the import price index is expressed as a percentage of the export price index the "price-ratio" thus obtained is a fairly good index of the terms on which a country obtains its imports in exchange for its exports. In the case of countries importing mainly raw materials and foodstuffs and exporting mainly manufactured goods, the lower the percentage figure the greater the advantage derived by them from selling manufactured products, and *vice versa*. On the other hand, in the case of predominantly agricultural countries importing manufactures and exporting raw materials and foodstuffs, the lower the percentage figure the greater the advantage derived by them from selling raw materials and foodstuffs, and *vice versa*. In order

[1] Haberler, *Prosperity and Depression*, p. 334, footnote.

to bring out the contrast between the predominantly agricultural and the predominantly industrial countries we give below the post-war price-ratios in the case of four countries, United Kingdom, India, Argentine and New Zealand, and we propose to discuss the nature of the change in the terms of trade, its bearing on the balance of international transactions and its repercussion on the external values of the currencies of agricultural countries in general and of the Indian currency in particular.

Price-ratio indices :

Year	*United Kingdom*	*India*	*Argentine*	*New Zealand*
1920	79	170	127	136
1921	70	164	157	131
1922	76	120	161	146
1923	75	131	151	108
1924	82	116	136	92
1925	84	103	116	87
1926	82	112	136	104

It is significant that the movement of the price-ratio index in the case of agricultural countries has been generally inverse to that in the case of industrial countries like the United Kingdom. During the early post-war years, owing to the greater increase in the prices of manufactured products than in those of raw materials and foodstuffs, the advantage as regards the terms of trade had been on the side of industrial countries. But between 1920 and 1925 the import and export price indices of States buying mainly manufactured goods and selling raw materials and foodstuffs were gradually approaching each other. The result was that "in India there was a rapid fall in the price ratio index between 1921 and 1925, and in Argentine and New Zealand, whose products are of a different order, between 1922 and 1925."[1] On the other hand there was a rise in the price-ratio index in the case of the United Kingdom; this meant that the advantage as regards the terms of trade gained by industrial countries was tending to disappear. But the most significant fact to be noticed is that in all the three

[1] *Memorandum on the Balance of Trade and International Payments*, 1913–27 (League of Nations), pp. 34–35 and p. 8.

agricultural countries there was a reaction in 1926, and the tendency was reversed to the disadvantage of agricultural countries in the very year that the rupee was stabilised at 1*s.* 6*d.*!

It would be a mistake to suppose that the reversal of this tendency simultaneously in the three agricultural countries was a chance coincidence. It is not necessary here to explain in detail the revolutionary changes in world agriculture during the period of post-war reconstruction. But there was undoubtedly one fact which was turning the terms of trade against agricultural countries, *viz.*, the extraordinary increase in the production of foodstuffs and raw materials. It appears from the *Memorandum on World Trade* published by the League of Nations in 1928 that the world's output of cereals and other food crops was 16 per cent higher in 1928 than in 1913, and that the corresponding increases for all foodstuffs and raw materials were 17 per cent and 48 per cent respectively. These increases considerably outstripped the rate of increase of the world's population. Mr. T. W. Lamont, in his address delivered before the New York Academy of Political Science, also pointed out that the average annual rate of increase of production during the period 1923–28 was 0·8 per cent in the case of cotton, 5·8 per cent in the case of sugar, 6·5 per cent in the case of rubber, 5·6 per cent in the case of copper, 5·1 per cent in the case of crude petroleum, and 4·9 per cent in the case of pig iron.

It would be instructive to examine more carefully the movements of the indices of export and import prices with particular reference to India.

Year	*Index of export prices*	*Index of import prices*	*Price ratio index*	*Balance of trade (crores)*
1919–20	158	206	130	+100
1920–21	140	237	170	+ 33
1921–22	127	214	164	+ 55
1922–23	140	169	120	+110
1923–24	145	190	131	+140
1924–25	154	180	116	+151
1925–26	152	158	103	+158
1926–27	132	148	112	+ 86

As already said, between 1920 and 1925 the export and import price indices in the case of India were gradually approaching each other with the result that she was getting gradually better terms for her exports of raw materials and foodstuffs. In 1925–26 the disparity between export and import prices almost disappeared, and the terms of trade as indicated by the price ratio almost reached the pre-war (1913–14) level. It is also significant that as the disparity became less and less the active balance of trade increased; in fact we discover a close negative correlation between the price ratios and the active balance of trade. All these tendencies apparently reflected a movement towards external equilibrium. But the fundamental change in the structure of world agriculture, which had led to a phenomenal expansion of production during the post-war period, and had been threatening the economic position of agricultural countries in relation to industrial countries in the sphere of international trade, was a factor of grave economic maladjustment that did not receive the attention that it deserved. It is very clear from the table given above that the export prices began to fall after 1924–25. In 1926–27 the index of export prices was 132 as compared to 152 in the previous year. In the *Review of the Trade of India* we find an official explanation that "the most important factor that contributed to this decrease was the *heavy fall* in the world prices of raw materials, particularly of cotton and jute." But unfortunately the fall in export prices was not viewed in the wider perspective of the causes which were threatening the external equilibrium of agricultural countries in relation to industrial countries and undermining the basis of India's active balance of trade (which is essential for debtor countries) and of her newly pegged exchange.

AGRICULTURAL COUNTRIES IN THE DEPRESSION

If our analysis of the world agricultural situation and of the position of agricultural countries *vis-à-vis* industrial countries is correct, then it appears that conditions were

ripe for a depression in world agriculture which was the most striking initial phase of the Great Depression that followed soon after. In the following years the agricultural depression was intensified by the universal and uninterrupted fall in commodity prices, and the pressure upon agricultural countries continued after the financial crisis of 1931. Since the beginning of 1931, however, the relation between the prices of manufactured products and the prices of primary products was not changing rapidly, to the disadvantage of agricultural countries. But there was no definite improvement of the terms of trade either in 1931 or the early part of 1932. "More specially the depreciation of the pound sterling had not the effect upon price relations that might have been expected."[1] By the middle of 1932 since the centre of gravity of the economic depression shifted from agricultural countries to industrial countries, there was improvement in the terms of trade of agricultural countries. But there was a reaction again after 1932. In the case of non-European agricultural countries the situation was aggravated by the increase in cereal exports (wheat, barley, rye and maize) from eastern to central and western Europe and a corresponding reduction in cereal imports into Europe from other continents. In fact agricultural protectionism and the growth of inter-European trade in agricultural products were important factors which adversely affected the position of non-European agricultural countries like India in the sphere of international trade.

The deterioration of the terms of trade of agricultural countries adversely affected the external equilibrium and the exchange stability of these countries. Most of these countries are debtors, and part of their exports, as in the case of India, may be regarded as payments on account of interest and dividends. "In 11 out of 15 typical agricultural countries the total amount spent annually during 1927–29 on the service of foreign debts and on dividend payments abroad was approximately a fifth of the average export value. Dividend payment naturally decreases when

[1] *Review of World Trade*, 1931–32 (League of Nations), p. 63.

business is depressed, but the bulk of the payments—for all debtor countries taken together probably two-thirds—represents fixed charges on long or short-term loans. The fall in the average export prices in terms of gold of five typical non-industrial countries between 1929 and 1930 was from 21 to 25 per cent, and between 1928 and 1930 about 30 per cent (India and New Zealand 27 per cent, China 29 per cent, Uruguay and Argentine 31 per cent), corresponding to an increase in the actual burden of the fixed debt charges of over 40 per cent."[1] Between 1929 and 1932 the average fall of about 60 per cent in the export prices of these countries meant a further increase in the real burden of debt payments in terms of gold currencies. Thus the debtor countries were forced to furnish a constantly increasing quantity of goods in order to meet the fixed external obligations. Simultaneously they were compelled to restrict their imports of manufactured products, and such restriction was brought about through a rise in the prices of manufactured goods relatively to those of agricultural products. Initially owing to the glut in the world market for agricultural products they had been unable to maintain the quantum of their exports. But when the quantum of their imports was restricted, the demand of industrial countries for foreign raw materials and foodstuffs was also reduced. Hence the quantum of exports of agricultural countries had a tendency to fall. In these circumstances the pressure to maintain their quantum of exports altered the barter terms of trade still more to the disadvantage of agricultural countries. Evidently they were in a vicious circle. As this process went on they found themselves in a serious predicament. Owing to the stoppage of international lending the balance of international transactions could not be modified in their favour by foreign loans. The quantum of imports could not be cut down beyond a certain limit. And they were failing to sell their products in quantities and at prices sufficient to meet their fixed obligations and simultaneously to cover their current needs for foreign goods.

[1] *Review of World Trade*, 1930 (League of Nations).

These countries attempted to reach external equilibrium generally in two ways, *viz.*, (1) exportation of gold, and (2) devaluation of their currencies. In 1930 a number of debtor countries were forced off the gold standard, while others tried to maintain the values of their currencies by means of exchange control which contracted imports and stimulated exports. In 1931 the abandonment of the gold standard by Great Britain and the consequent depreciation of sterling involved some relaxation in the burden of debt of certain countries. But the adjustment of the trade balances of agricultural countries urgently required an increase in their competitive power, and this was possible through a reduction of the gold prices of their exportable commodities. As between deflation and currency devaluation, almost without exception they chose the latter as the best method of maintaining external equilibrium and the stability of the external values of their currencies. But the important question which we must now answer is, what has been India's choice of alternatives? Deflation, or currency devaluation?

The movement for currency depreciation gathered momentum since 1930 "till by the beginning of 1933 the foreign trade of the countries with depreciated currencies represented about 52 per cent of world trade. By the end of April 1933 when the U.S.A. dollar depreciated the share increased to 64 per cent. The remaining 36 per cent represented the trade of countries adhering to an effective gold standard (about 20 per cent of world trade) and of countries maintaining an approximate gold parity of their currencies by means of exchange restrictions (about 16 per cent of world trade)."[1] India joined this general movement under the leadership of Great Britain. When Great Britain abandoned the gold standard the rupee, being linked to sterling, naturally depreciated in terms of gold. Hence those who are clamouring for the devaluation of the rupee have been told that since the rupee has already been subject to devaluation like the currencies of countries forming the sterling bloc, India has actually obtained

[1] *Review of World Trade*, 1932 (League of Nations).

whatever relaxation or relief may have been secured by other agricultural countries through currency depreciation. Unfortunately such an argument is complacently advanced, and sometimes equally complacently accepted, without discrimination, and it is necessary to examine whether facts furnish a solid ground for such self-complacency.

EXCHANGE DEPRECIATION IN RELATION TO PRICES, TRADE AND PRODUCTION

Theoretically, moderate depreciation of the foreign exchanges—as opposed to depreciation caused by hyper-inflation and accompanied by economic dislocation, as during the Great War—provided the exchange rate is approximately kept stable at a new lower parity, acts as a bounty on exports and as an *ad valorem* restrictive duty on imports. As internal costs and prices adjust themselves to the exchange depreciation the extent of the bounty on exports and the restrictive effects on imports are, no doubt, *pro tanto* reduced. But there is a permanent advantage in foreign trade to the extent that certain internal costs, such as long-term interest and rent charges (and to a smaller extent various tax charges) which form important elements of cost in Indian agriculture and are fixed in terms of money, fail to rise. Moreover even supposing that most of the direct advantage of depreciation is temporary, since currency depreciation in a period of depression has that kind of expansionary and recuperative effect upon internal economy which is cumulative in its momentum, it has ultimately an expansionary effect upon both exports and imports in the long period. Hence it is wrong to suppose that all the effects of exchange depreciation necessarily exhaust themselves in the short period.

What have been the effects of currency depreciation on the foreign trade of countries with depreciated currencies in general and of India in particular? Professor James W. Angell of Columbia University has given us an admirable survey of the general effects of currency depreciation on foreign trade in his address delivered before the Academy

of Political Science in 1933.[1] It is obvious that these effects cannot be isolated from the contemporary economic phenomena and tendencies, such as the deepening of the economic depression, protectionism, development of economic autarchy and the erection of various kinds of trade barriers. As Professor Angell points out, on account of the deepening of the economic depression "nearly all of the phenomena at issue must be measured in terms of a shrinking base."[2] Moreover, to the extent that tariffs and import restrictions were employed by the gold bloc to shut out imports from countries with depreciated currencies, the expansionary effect of devaluation on exports of the latter was neutralised. Nevertheless on the basis of available data we can reach some general conclusions with confidence. For purposes of comparison the "stable" countries selected by Professor Angell are Austria, Belgium, Czechoslovakia, France, Germany, Holland, Italy, Poland, Switzerland and the United States of America, while countries with depreciated currencies selected by him are Denmark, England, Norway, Sweden, British India, Argentina, Canada, Chile, China, Japan, Mexico, Peru and Spain. In the case of the latter exchange depreciation has been, on the whole, moderate; "the average foreign exchange rate in December, 1932, stood at 69·4 per cent on the gold par, with a range for the group between a low of 42 and a high of 91."[3] But it must be noted that, in spite of exchange depreciation, the level of wholesale prices and the cost of living indices in these countries were virtually the same in 1932 as in 1931. In the ten principal "stable" countries the average wholesale price level for 1932 stood at 89 per cent of 1931 and the average cost of living index at 93. But for eleven of the "depreciated countries" the average wholesale price level in 1932 stood at 103 per cent of 1931 and the cost of living index at 98.[4] The remarkable stability of wholesale prices and cost of living in countries

[1] *Proceedings of the Academy of Political Science*, Vol. XV, June, 1933. Professor G. W. Angell's address on Exchange Depreciation, Foreign Trade and National Welfare.

[2] Ibid., p. 11.

[3] Ibid., p. 12.

[4] Ibid., p. 13.

with depreciated currencies implied a *relative rise* when the indices were falling very sharply in the countries of the gold bloc. "Had the average price index for these depreciated countries risen in full proportion to average exchange depreciation, with prices in the stable countries taken as the base, it would have reached 128. The adjustment of internal prices to the new exchange levels which usually appears in due course was, hence, only about a third completed by the end of 1932."[1] Thus here we come across a typical problem of the short-period effects of moderate exchange depreciation on foreign trade. The relevant facts bearing on this problem are embodied in the following comparative table. The figures for export and import values of "stable" and "unstable" countries have been taken from the table compiled by Professor Angell, while for purposes of comparison and contrast from our point of view we have worked out the comparable data for India, Canada, Argentina, and England.[2]

VALUES:

	Stable (10)	*Unstable* (13)	*India*	*Canada*	*Argentina*	*England*
Imports:						
1932 Imports as percentage of 1929	42	50	52	35	43	58
1932 Imports as percentage of 1931	69	77	98	73	71	80
Average	56	64	75	54	57	69
Exports:						
1932 Exports as percentage of 1929	40	51	42	45	59	50
1932 Exports as percentage of 1931	60	85	82	87	89	93
Average	50	68	62	66	74	71
Average for total trade	53	66	68	60	66	70

[1] *Proceedings of the Academy of Political Science*, Vol. XV, p. 13.
[2] Ibid., p. 14, footnote.

VALUES—*continued:*

Index of Industrial Production:	*Stable* (8)	*Unstable* (5)				
1932 as compared to 1929 1931 Average	—32	—11	—	—	—	— 8

It will be observed that the conclusions drawn from theory are definitely confirmed by facts. As regards imports the average total money value in 1932 was 56 per cent of the base figure in the case of countries with stable currencies, while it was only 64 per cent in the case of countries with depreciated currencies. On the other hand, the average total value of exports dropped to 50 per cent of the base in the case of "stable" countries and to 68 per cent in the case of "unstable" countries. Thus when we take a broad base, *viz.*, the average of 1929 and 1931, we reach several interesting conclusions. First, the decline in the value of the total foreign trade as well as of imports and exports taken separately was much less in the case of "unstable" than in the case of "stable" countries. Secondly, the decline in exports was greater than the decline in imports in "stable" countries, while the decline in exports was less than the decline in imports in "unstable" countries. Thirdly, as regards the expansionary effects of exchange depreciation in industrial production, it seems that the decline in industrial production or deflationary contraction caused by the economic depression was very much greater in "stable" than in "unstable" countries. From the point of foreign trade also the decline (in both import and export trade) was arrested to a much greater extent in "unstable" than in "stable" countries. And it is particularly remarkable that in 1932 the average total value of exports was as high as 85 per cent of that in 1931, in the case of unstable countries, and only 60 per cent of the average total export value of 1931 in the case of "stable" countries. On the whole, therefore, it cannot be seriously contested that, although there was no positive economic recovery in the unstable countries, yet exchange depreciation operated as a definite anti-cyclical force in

these countries, counteracted the general process of deflationary contraction, and helped them to maintain equilibrium in the balance of international transactions by means of a relative expansion, or, to be more accurate, a less rapid contraction of their export trade.

INDIA AS COMPARED TO OTHER AGRICULTURAL COUNTRIES AND ENGLAND

Now let us analyse the position of India as compared to two other agricultural countries which were similarly situated and also as compared to England whose currency management determined the direction of Indian currency developments under the sterling exchange standard. In the case of Canada and Argentina there was a drastic reduction of imports, so that in 1932 the average total value of imports was respectively 54 per cent and 57 per cent of the average of 1929 and 1931. But the comparable figures for the average total export values are 66 per cent and 74 per cent respectively. This means that the situation as regards foreign trade was conducive to external equilibrium. In the case of India curiously enough the situation was different. It is remarkable that the average total import values in 1932 amounted to as much as 75 per cent of the average total value for 1929 and 1931. This is the highest of the comparable figures in the whole table. In other words the reduction of imports was the least when we compare her with "unstable" countries in general and agricultural countries in particular. On the other hand, when we compare export values we are equally struck by the fact that in the case of India the decline in exports was more than in "unstable" countries generally, a little more than in Canada and considerably more than in Argentina. Moreover, it appears that, after the abandonment of the gold standard by England, the decline in imports into India was arrested to an unprecedented extent, the import values in 1932 being virtually the same as the import values in 1931. At the same time, the decline in exports between 1929 and 1932 was almost as much as the

decline in the exports of the countries of the gold bloc. After the depreciation of the exchanges the fall in exports was arrested to a much greater extent in India than in the gold standard countries. But it is obvious that this fall was arrested to a smaller extent in India than in "unstable" countries generally and other agricultural countries particularly. On the whole, facts clearly show that India resembled "stable" rather than "unstable" countries in two important respects: (1) The decline in exports was much greater than the decline in imports; and (2) there was a very heavy decline in exports between 1929 and 1932, the extent of the fall in exports being almost the same in India as in "stable" countries. Hence the situation as regards foreign trade was hardly conducive to external equilibrium which had been threatened with the onset of the depression and even earlier. Nor was this all; the situation was aggravated further by the maintenance of imports at a much higher level than in countries with depreciated currencies and in countries with stable currencies. In fact the average total import value in 1932 was as much as 75 per cent of the average for 1929 and 1931.

When we compare and contrast the effects of currency depreciation on external equilibrium in the case of India with those in the case of England we reach certain conclusions which have an important bearing on the recent ratio controversy. As every student of modern currency history knows, the immediate cause of the failure of the gold standard in England was the withdrawal of foreign balances on a tremendous scale, while her foreign assets were frozen and unrealisable. But as Sir Walter Layton says, "that is only part of the story, for behind this capital flight was the fact that during the preceding year our (*England's*) *national trading account had been getting more and more out of balance.*"[1] England was buying more than

[1] An address on International Co-operation delivered by Sir Walter Layton, C.B.E., C.H., in June, 1933, before the American Academy of Political Science (*Proceedings of the Academy*, pp. 74–76). We have quoted extensively from this address specially because Sir Walter Layton is a recognised authority on currency and finance and his opinions are regarded as authoritative not only in Great Britain but also in India.

she could sell, and one of the most important reasons why the balance of accounts was moving against her was that she was "almost the only remaining free trade country in the world surrounded by a ring of tariffs which were rising higher and higher." So long as the stream of international lending did not dry up, it was possible for her to meet the situation by foreign borrowing. But when international lending ceased "it became imperative to balance our (England's) current account, which meant that by some means or other our (England's) imports must fall or our (England's) exports increase. There was no other possibility." Thus fundamentally England had found herself in the category of agricultural countries like India who had been struggling hard to maintain equilibrium in the balance of international transactions earlier than the economic crisis of 1931. Now what means were adopted in England for restoring external equilibrium? The most important instrument for restoring external equilibrium was the devaluation of sterling. "When the pound fell it settled down after a while at a level which has gone a long way toward restoring equilibrium in our balance of payments," and "the level to which the British exchange fell was largely determined by the level of the tariffs and the severity of other restrictions which were existing against British trade."[1] Here we have a conspicuous example of rational currency management based on the manipulation of the exchange rate with a definite objective. Thus the level of the pound, which was maintained by means of the Exchange Equalisation Fund, was, in the words of Sir Walter Layton, "a level determined by the existing situation of international trade barriers and all the concomitant series of conditions which determine trade. It was, therefore, not a level which we chose but, in a sense, a *natural level*."[2] The success of the British currency policy was not long

[1] The process of external equilibrium was also helped by protectionism and subsequently by the operation of the Ottawa Agreement.

[2] We wish the currency experts of the Government of India had this notion of the natural level of the rupee.

It may be mentioned here that the principal object of maintaining equalisation accounts has been to offset influences operating through the balance of international payments on the internal economic structure.

delayed. If we examine the statistics in the table given above we observe (1) that the level of exports in 1932 was maintained at 71 per cent of the average for 1929 and 1931 and at 93 per cent of the exports of 1931; and that (2) there was only 8 per cent decrease in the index of industrial production as compared to an average of 32 per cent in the case of gold-standard countries, and 11 per cent in the case of countries with depreciated currencies taken as a whole. Gradually the internal strength and stability of sterling, which was reinforced by a number of countries, particularly India, linking their currencies to sterling, asserted itself, and gold began to flow back from many countries of the gold bloc to the sterling area.

It must not be supposed that these results were brought about by a dose of active internal inflation caused by expansion of currency and credit. After the abandonment of the gold standard the wholesale prices as well as the quantity of currency and bank deposits in England were remarkably stable. But since internal prices in gold-standard countries were declining rapidly and soon fell by 10 to 20 per cent there was a *relative rise* of internal prices in England which had an expansionary effect on business activity. Hence, as Sir Walter Layton points out, "though we may be solvent internationally in the sense of paying our way and balancing our accounts, both our incomes and outgoings are extremely low; *and we are faced with the problem, as everybody else is faced, of raising the price level.*" But a rise of internal prices in England through reflation was keenly anticipated in all the countries of the sterling area. In fact the expansionary effect of reflation in England would have transmitted itself more easily to the sterling bloc and would have gone farther than under gold-standard conditions. But in England, as Hawtrey, says, "the opportunity had been lost, deflation and falling prices prevailed in spite of the abandonment of gold, and the pound sterling had become a currency only one degree less intolerable than gold itself."[1] The policy of easy money adopted later came too late, because the

[1] Hawtrey, *The Gold Standard in Theory and Practice, 1933*, p. 185.

vicious circle of deflation had already been rejoined. Whether a reflationary policy would have suited British economic interests and needs was an open question or "problem" as Sir Walter Layton puts it. Perhaps internal inflation in England immediately after the abandonment of gold would have made it impossible to maintain the strength and stability of sterling in relation to gold. But agricultural countries like India which have to bear a heavy burden of external obligations were not on the same footing as England and did not obviously desire that the deflationary effect of the English currency policy should transmit itself to their internal economic structure through the sterling link. Sweden, for example, took the necessary step and readjusted her exchanges in relation to sterling to suit her own special needs. Thus it is interesting to note that exchange control in Sweden "was not only secondary to, but was actually employed as a means toward internal stabilisation. The pound at first depreciated more rapidly than the Krona, and in October, 1931, was quoted 7 per cent below Krona parity. This was consistent with Sweden's determination to prevent inflation. In December, 1931, the old Krona-pound parity was almost restored, and beginning April, 1932, in accordance with Sweden's desire to reflate wholesale prices, the pound was quoted about 7½ per cent above par, except for the period from November, 1932, to March, 1933, when the old parity with the pound was temporarily re-established."[1]

India was unfortunately not free to strike out a path of her own. The rupee had to trim its sails to the winds of sterling. Hence with the rupee-sterling ratio pegged at the same level, the sterling link transmitted very easily the deflationary effect of the British currency policy. But what is more tragic is that the internal economic structure of India had to go through a grinding process of price deflation which was without any parallel in the sterling area. As already emphasised, from 1931 onward the price level in countries with depreciated currencies remained stable; the decline was stopped, and was followed

[1] Fisher, *Stabilised Money*, p. 400.

by a rising tendency after a year or two. In India immediately after the devaluation of the rupee in terms of gold the index number of prices moved up from 91 in September, 1931, to 98 in December, 1931, when the depreciation in terms of gold was the highest in the case of the rupee and the pound. But after December, 1931, the rise of prices was counteracted, and after the close of the year 1932 prices began to fall below the level of September, 1931. The index number reached the lowest level of 82 in March, 1933. Between March 1933 and 1937 there was no further decline; nor was there any appreciable upward movement. On the other hand, as early as 1935 there was a definitely upward movement of prices in *all except the gold standard countries*, and the divergence between the national price levels was closing up in the case of most countries. On the whole, we find that India's external equilibrium was threatened in the same way as the external equilibrium of countries adhering to the gold standard. And it is sad to reflect that in India exchange control was not employed, as in Sweden, "as a means toward internal stabilisation." Nor was it employed, as in Great Britain, as an instrument of "restoring equilibrium" in the balance of trade which was being threatened as the result of the disparity between import and export prices since 1926.

ECONOMIES OF GOLD EXPORTS

Since currency management failed at a crucial moment to restore external equilibrium through a readjustment of the trade balance India had to resort to gold exports in order to maintain equilibrium in the balance of international transactions. Exportation of gold from India in recent years has been commonly regarded as a unique economic phenomenon. The phenomenon is certainly unique when we come to think of the volume and continuity of the outflow of gold and observe how the rôle of India as a habitual importer of gold has been suddenly reversed.[1] But fundamentally

[1] According to a statement recently made by the Finance Member in the Assembly since Great Britain went off the gold standard gold to the

the phenomenon was not unique in so far as her position was essentially the same as that of many debtor countries with gold-standard currencies who had eventually to go off gold and resort to currency depreciation as the only means of avoiding national bankruptcy after the financial crisis of 1931. Ever since the first half of 1929 when France withdrew her foreign short-term assets and a period of contraction of foreign lending began, many debtor countries with gold standard currencies were forced to counter-balance the change in the credit situation by repeated gold exports. When by the middle of 1931 international capital movements were completely arrested as the result of the financial crisis, the gold reserves of numerous debtor countries were largely depleted, and the only alternative left for them was devaluation of their currencies. From the end of 1932 to September, 1936, we observe a reversal of gold movements, *i.e.*, a flow of gold from the gold bloc to the sterling area.[1] The fundamental causes which induced the reversal of the gold movements were the same. Exchange depreciation in the sterling area exerted a deflationary pressure on internal prices in the gold-standard countries, and restricted their exports, while stimulating imports from countries with depreciated currencies. Hence those countries which did not resort to drastic exchange control and import restrictions were faced with disequilibrium in the balance of international payments and began to export gold in fairly large quantities.[2]

The mechanism of gold exports has brought into sharp relief some of the fundamental features of Indian cur-

value of Rs. 326 crores has been exported from India. According to a tentative estimate given in the annual report of the Bank of International Settlements for the year 1934–35 gold hoarded in India from 1893 to 1930 amounted to a minimum of Rs. 1,454 crores. Of this amount 22·4 per cent has been exported since 1931.

[1] Gold was lost by Netherlands, Switzerland, Italy and most of all by France, and was acquired by U.S.A., United Kingdom, Sweden, Norway, S. Africa, Portugal, Egypt, Finland and Belgium.

[2] It should be noted that countries with depreciated currencies also resorted to purchase of gold as a method of maintaining their foreign exchanges at a low level in terms of gold. For example, the Swedish Riksbank increased its gold holdings by 164 million Kroner between March, 1933, and December, 1933, with this object in view.

rency management during the Great Depression. It may be recalled that gold exports were induced first by the very act of the devaluation of the rupee in terms of gold which at once raised the rupee-price of gold. Since gold is a commodity which is universally acceptable, the demand for which has increased greatly due to rise of liquidity preference caused by the Depression (there being an upward shift in the demand curve for gold, and which has not to encounter trade barriers in the course of its passage from one country to another, the exports of gold were at once stimulated particularly at a time when the value of agricultural products (which we export) in terms of industrial products (which we import) had fallen to the detriment of our active balance of trade. Had there been a reflationary rise of domestic prices immediately (1) either by prohibiting the exports of gold and commandeering private hoards and converting them into a basis of expansion of paper money, as was done in America, or (2) by expansion of currency even when retaining the sterling link, the outflow of gold would have slowed down and would have been eventually arrested altogether. But, as already pointed out, there was heavy price deflation in India which heightened the deflationary effect of the economic depression and broadened the difference between the external price and the rupee price of gold. To elucidate this statement we would emphasise an important peculiarity of the dishoarding of gold in India. It is very often ignored that gold for export has come not from the currency reserves of the central bank as in other countries but from private hoards. In India these private hoards of gold have represented a form of capital asset like land from time immemorial. Under deflationary pressure the agricultural population have been compelled to part with these assets. Thus dishoarding of gold is merely the effect of debt liquidation which is a universal phenomenon connected with the process of economic contraction. When the contraction process has already set in, a debtor when he is pressed to repay a loan "is not always in a position to meet his obligation out of his current receipts. Ordinarily he will be forced to sell assets

in order to raise the fund for the discharge of his debt. He may sell securities, real estate, or commodities of different descriptions. These forced sales must have a depressing influence on the price of the assets with deflationary consequences."[1] There is no doubt that in India the bulk of the internal sales of gold have been forced sales which have had a depressing influence on the rupee-price of gold thus widening the difference between the internal and the external prices of gold and stimulating gold exports in unusual quantities.

The maintenance of the rupee-sterling link at 1*s.* 6*d.* to the rupee concurrently with heavy internal price deflation has constituted a conditioning factor of gold exports. As the result of the internal appreciation of the rupee, its external purchasing power remaining the same, the rupee was undervalued in relation to sterling. According to the *League of Nations' Report on Commercial Banks*, 1929–34, the extent of the undervaluation of the rupee was 10·31 per cent, in 1931, 15·04 per cent in 1932, 16·18 per cent in 1933, and 18·23 per cent in 1934. As already pointed out, since prices in India remained consistently low between 1934 and 1937, whereas there was an upward movement in other countries after 1935, the undervaluation of the rupee increased still further. Thus the state of the exchanges was such that the rupee price of gold was lower than its sterling price expressed in rupees at the prevailing rupee-sterling market rate. But it must be borne in mind that undervaluation of the rupee was merely a conditioning factor in the process of gold exports, a reflection of the internal overvaluation of the rupee due to heavy price deflation. It is interesting to speculate how internal price deflation could be maintained in the face of the external undervaluation of the rupee and thus turned out to be the predominant factor in the Indian economic situation. First, owing to the upward shift in the demand curve for gold as compared to the demand curve for particularly agricultural products during the depression, the undervaluation of the rupee had an expansionary effect on gold exports rather

[1] Haberler, *Prosperity and Depression*, p. 235.

than on commodity exports. Secondly, the forced sales of capital assets like gold and also land have intensified the economic depression in the countryside. In so far as the sale proceeds of gold converted into negotiable securities have formed the basis of new bank deposits, or cash has been dishoarded to buy gold, an expansionary effect of gold sales is conceivable. But it is doubtful whether gold exports have increased financial circulation and contributed to internal expansion to any appreciable extent. Lastly, it is not inconceivable that the currency authorities pursued an active deflationary policy which was indispensable for a smooth working of the mechanism of the dishoarding and export of gold.

It is not contended here that gold exports *per se* have led to economic disaster. We are inclined to agree with Keynes when he says that "in time of peace to substitute goods for gold when goods are cheap in terms of gold and gold for goods when goods are dear in terms of gold will be both socially and financially profitable."[1] But what we condemn is the fundamental cause of gold exports, *viz.*, the heavy price deflation which has made the rupee a currency which has been perhaps as intolerable as gold and not "a currency only one degree less intolerable than gold itself," as Hawtrey characterised the pound sterling after September, 1931.

The above survey of the nature and methods of currency stabilisation in India in the post-war period reveals a rationale of currency management which demands the closest scrutiny at the present juncture. In India the principle of stabilisation that has been traditionally followed is the principle of exchange stability. It is obvious that if the exchange-rate is maintained at a particular level which is regarded as the basic norm, the internal economic structure is exposed to economic fluctuations originating in other countries—fluctuations which may be not only of the nature of secular dynamic changes in economic life but also short-run fluctuations within the secular trend which

[1] Cf. a paper recently read before the Economics Section of the British Association.

it has been the ordinary task of monetary authorities in the post-war world to moderate by deliberate devices. In the pre-war world of international gold standard and comparative freedom of trade the operation of the gold standard guaranteed, within limits, stability of prices as well as stability of exchanges. There used to be a fixed purchasing power parity based on gold parity which maintained the national price levels fairly in harmony with one another. Both international equilibrium or harmony of national price levels and the adjustment of the internal structure of prices, production, wages and other money incomes to the fixed purchasing power parity were achieved to an appreciable extent through a fairly flexible economic system, a fairly flexible equitable distribution of gold and a fairly smooth working of the international gold standard. Under these conditions exchange stability more often than not secured price stability. But in the present day world conditions are just the reverse. Thus we observe the phenomena of closed economic systems based on more or less self-sufficient and rigid economic structures; of systems insulated against external economic pressure and disturbances by exchange depreciation, exchange control and tariff and other trade barriers; of acute disharmony of national price levels; and of fluctuating purchasing power parities. These fundamental changes are due, among other things, to the breakdown of the international gold standard. Under these changed conditions the maintenance of exchange stability has exposed India's internal economic structure to grave international maladjustments which have shaken the foundations of world economy in recent years, and has profoundly disturbed her external equilibrium. In this respect her currency policy has run counter to both enlightened economic theory and actual practice.

RATIONALE OF POST-WAR CURRENCY MANAGEMENT

Judged from this point of view post-war currency stabilisation in India has betrayed its inherently artificial character. The attempt to stabilise the rupee at 2*s.* gold in 1920 was

a dismal failure because the catastrophic fall of external prices, which was transmitted through an overvalued rupee, was too much of a disturbance to be tolerated by our internal economic structure and price system. The subsequent decision to leave the exchange-rate to find its own level had a salutary effect upon our internal economy. As Keynes testified before the Hilton-Young Commission the currency authorities by abstaining from exchange pegging at a time when world prices were in serious disequilibrium protected the internal economic structure to a certain extent against the fluctuations in gold prices during the boom of 1929–30 and the slump of 1921–22. During the ratio controversy of 1926 foreign as well as Indian experts urged with commendable foresight that since national price levels were still out of harmony and were still fluctuating the currency authorities should sit on the fence and await developments. But if they stabilised the rupee without "maintaining legislative freedom to adjust her exchange to the events in the outside world and so preserving the stability of her internal prices" they might be guilty of importing serious instability into the costs-prices structure if world prices fluctuated later. Sir Basil Blackett must have toyed with the ideal of price stability; otherwise it is amazing that he should have sought to prove that exchange-stability at the *de facto* rate of 1*s.* 6*d.* implied also internal price stability on the ground that British, American and Indian prices had somehow "come together at a figure about 160," and that he should not have taken the elementary precaution suggested by Keynes and other Indian and foreign witnesses. The fact is that the movement for stabilisation in India was inspired, if not dictated, by the restoration of the gold standard in Great Britain in 1925. But, as events have amply demonstrated, stabilisation was ill-advised and inopportune in both countries. As Sir Walter Layton says, "The mistake that we made in 1924 was to endeavour to set up an international monetary system without first making sure that the economic background was right." We do not know how the "economic background" was studied in England; but it is amazing

that in India so much was made of the accidental parity of British, American and Indian prices and that such exaggerated emphasis was laid on measurements of purchasing-power parity based on comparisons of price levels as if these afford reliable criteria of overvaluation or undervaluation of a country's currency. At any rate, as Keynes has shown, the pound sterling became overvalued in relation to gold after 1925 and exercised a deflationary effect upon England's foreign trade and dislocated her internal economic structure.[1] In India the link of the rupee with the overvalued sterling transmitted the fall of sterling prices between 1924 and 1929 to the Indian price system, and created internal instability of prices not only absolutely but also relatively to prices in countries which were the best customers of India. So far as external equilibrium was concerned it was also threatened by a fundamental change in the barter terms of trade which manifested itself in 1926–27 and was subsequently reflected in the steadily shrinking active merchandise balance of trade in later years thus threatening the equilibrium of India's balance of international payments.

During the years of depression the twofold disturbance to which Indian economic life was exposed after the currency stabilisation of 1927, *viz.* (1) internal price instability manifesting itself in heavy price deflation and (2) shrinking of the active merchandise balance of trade, was accentuated first by the agricultural depression and then by the industrial slump. Such maladjustment was not peculiar to either Great Britain or India. But a dispassionate survey of facts given above demonstrates very clearly that while Great Britain and agricultural countries like Australia and Sweden had succeeded, after the abandonment of the gold standard, in stabilising internal prices by reflationary adjustment or at least by arresting the avalanche-like fall

[1] Cf. Keynes, "Economic Consequences of Mr. Churchill." In an addendum to the Report by a Court of Enquiry concerning the Coal Mining Industry Dispute, 1925, Sir Josiah Stamp dissented from his colleagues in coming to the conclusion that the main causes of the troubles in the British Coal Mining Industry were deflation and England's return to gold.

of prices and in restoring external equilibrium through an absolute or at least relative rise of prices combined with the devaluation of their currencies, India has pinned her faith on the traditional policy of exchange stability which has transmitted the devastating deflationary shocks of the world economic depression to her internal economy.

DIVERGENCE BETWEEN PROFESSION AND PRACTICE

Curiously enough we find a divergence between profession and practice in the realm of monetary policy both in the case of Great Britain and India. At the Imperial Economic Conference held in Ottawa in 1932 authoritative pronouncements were made by representatives of the Empire countries on the question of monetary policy. The Conference was held to lay the foundations of inter-Imperial stabilisation of commercial and monetary relations. At this Conference Sir Henry Strakosch, Member of the Council of India, while enunciating the Imperial monetary policy, declared: "Pending the re-establishment of a stable international monetary standard the Empire countries should as far as possible adopt a common standard of value, and the wholesale level of prices in terms of that common standard should be raised to a point at which an equilibrium is re-established between costs and that level of prices. Further, on the attainment of that level, monetary policy should be directed towards maintaining it stable both in terms of commodities and in terms of other Empire currencies. The United Kingdom being the greatest centre for Empire trade and finance, and being in a very strong creditor position *vis-à-vis* the rest of the Empire, the trend of prices in terms of the common standard must depend in the main upon the monetary policy she decides to pursue."[1] We cannot imagine a more clear enunciation of the policy of a reflationary rise of prices with the object of re-establishing the costs-prices equilibrium. It is obvious that Sir Henry regarded the costs-prices equilibrium as the fundamental basis of stabilisation and exchange-

[1] Imperial Economic Conference, 1932. Report to the Conference, p. 142.

stability as an objective which must be subordinate to, and consistent with, costs-prices equilibrium. Had this rational monetary policy, so ably stated by one of the accredited representatives of India, been only partially followed by the Government of India, India's economic travail during the depression would have been mitigated to a considerable extent. Sir Henry Strakosch gave a broad hint that Great Britain should take the lead in reflationary readjustment. The leader of the New Zealand delegation put the issue more clearly when he said: "We can make some local adjustments, but it is simply impossible to restore even a reasonable measure of sound conditions in the Dominion unless and until the general price level in Great Britain is increased, and *increased substantially*. That is something which cannot be left to take care of itself."[1] The response of Mr. Neville Chamberlain, Chancellor of the Exchequer, was no less clear and emphatic. He said: "I want to make it perfectly clear at once that upon the desirability of raising wholesale commodity prices the United Kingdom Delegation is in full sympathy and agreement with the Dominions and India."[2] At the London Economic Conference held in 1933, which broke up as the result of a clash of monetary policies, the United States of America and Sweden wanted to reflate their domestic price levels before stabilising exchange; while France, England and some other countries favoured a temporary exchange stabilisation prior to domestic reflation. We need not go into the merits of the two policies. But there is no doubt that both parties did want a reflationary adjustment of prices with a view to restoring the costs-price equilibrium. In spite of the failure of the Conference it is significant that Great Britain and the majority of the countries belonging to the "Sterlingaria" reiterated the policy enunciated at Ottawa, and signed a so-called Imperial Declaration which said that *a continued rise in commodity prices was most desirable in order "to restore the activity of industry and employment, insure an economic return to the producer of primary commodities, and harmonise*

[1] Imperial Economic Conference, 1932. Report to the Conference, p. 126.
[2] Ibid., p. 143.

the burden of debts and fixed charges with economic capacity."[1] Indians hardly realise that what they have been demanding for such a long time and even now (of course very often with a wrong and perverted emphasis) is incorporated in an Imperial Declaration which the Government of India was, and still is, morally bound to respect and implement.[2]

Subsequent events have shown that Great Britain has paid only lip homage to the ideal of reflationary stabilisation of sterling prices. Mr. Reginald McKenna who was so enthusiastic about the Imperial declaration believed that the signing of this declaration by England placed upon the Bank of England the responsibility of initiating a new monetary policy. But price reflation has not gone so far as it should have gone in the interests of Imperial economic stability without which Imperial monetary unity has little meaning. Nevertheless, Great Britain has solved her domestic problems more or less successfully. The devaluation of the pound after September, 1931, in so far as it corrected its previous overvaluation in terms of gold had an obvious expansionary effect upon industry, trade and employment. As Sir Walter Layton says, by means of devaluation the continuing pressure of an adverse balance of trade was removed, and external equilibrium regained. But the central feature of British currency management during the depression is imperfectly realised in this country. In the words of Sir Walter Layton, which bear repetition, the pound has been allowed to find a "natural level"—a level determined by "the existing situation of international trade and all the concomitant series of conditions which determine trade." Moreover, influences operating on the internal economic structure through the balance of international payments are offset by the operation of the Exchange Equalisation Fund. Thus there is no rigid exchange stability which is regarded as sacrosanct and as an unalterable basic norm. Although no country understands the

[1] Fisher, *Stabilised Money*, p. 359.

[2] Mr. Reginald McKenna, in the *Midland Bank Monthly Review*, January–February, 1934, expressed the opinion that "This declaration may well prove the most important profession of faith the world has yet had on the subject of monetary policy."

need for maintaining reasonable exchange stability better than Great Britain, yet there is at the same time a keen anxiety not to over-emphasise the claims of exchange stability to the detriment of the internal costs-prices structure.

Other countries of the "Sterlingaria" for want of a definite lead from Great Britain in the shape of a "substantial rise" of sterling prices appear to have fallen back upon a domestic solution of their particular monetary problems. For example, as already pointed out, Sweden pursued an independent policy of reflationary stabilisation of internal prices and stabilisation of the cost of living even at the expense of exchange stability in relation to sterling, thus insulating her internal economic structure almost completely and effectively against the world depression.[1] The basis of this policy was to make "wise adjustments of foreign exchange operations to the domestic requirements of the country; that is, purchasing foreign exchange to maintain a low foreign valuation of the Krona; abandoning the exchange stability of the Krona with the English pound when such exchange stability tended to pull down the Swedish price level; but maintaining a stable sterling exchange when the beneficial influence of a rise of British wholesale prices could thus be made to effect a corresponding rise of the Swedish wholesale price level."[2] In Australia the gold standard was abandoned in November, 1929, in order to permit her "the full use of her gold reserves to meet external obligations"—a course of action similar to what India adopted after September, 1931.[3] But eventually Australia resorted to considerable devaluation as a reflationary measure, and the depreciation "proceeded to a point where 185 Australian paper pounds were equivalent to 100 gold pounds, that is, the price of gold was raised 85 per cent."[4] On the other hand, India has persistently clung to exchange

[1] This shows, as Dr. Fisher maintains, "that the foreign exchange value of the Krona was determined independently of the pound, that is, Sweden did not properly belong to the 'Sterlingaria' group." (*Stabilised Money*, p. 400.)

[2] Fisher, *Stabilised Money*, p. 330.

[3] Ibid., p. 334.

[4] Ibid., p. 338.

stability at the cost of internal price stability—a policy which has, as we have shown, led to unprecedented price deflation and paralysis of economic activity and is warranted neither by the professions of her accredited representatives nor by the theory and practice of post-war currency stabilisation.

REAL CASE FOR DEVALUATION

The case for the devaluation of the rupee presented above in the context of long-run tendencies and the fundamental maladjustments of our national economy, and from the point of view of the post-war monetary theory and practice, has been stated in such a manner as to clear up the radical issues involved in this controversy. This is not really a narrow issue between an historic norm of 1*s.* 4*d.* and the norm of 1*s.* 6*d.*, which has become equally historic. The issues are much wider. Do we want price stability or exchange stability in the abnormal circumstances of the post-war world? Devaluation being a means to an end, *i.e.*, an instrument of monetary stabilisation, is devaluation enough to secure a reflationary stabilisation of the internal price level and get rid of the heavy price deflation which has paralysed the economic life of the country? Or should it be supplemented by other measures? Do we want a national solution of the problem of price deflation by insulating our internal economy against external disequilibrium? Do we want alterable exchange parities and the freedom to adjust the ratio according to the fundamental needs of our national economy? Do we want the exchange-value of the rupee to fall in the same way as Great Britain has recently allowed the sterling-dollar rate to fall from the historic par of 4.86 to about 4·66 in the course of a few months in order to correct the overvaluation of sterling and thus to improve her export trade? These are the fundamental questions involved in this controversy. And we have already indicated the manner in which these questions ought to be, and have actually been, answered, particularly by agricultural countries similarly situated as India.

Unfortunately the question of devaluation has been

recently debated against a narrow background of the recent trade recession and the difficulties of the currency authorities in the face of sagging exchange. Such a procedure is apt to cloud the wider and more vital issues. If, for example, it is proved that the present ratio should not be altered on fundamental grounds and that it has a tendency to secure external and internal equilibrium in a fundamental sense, then there is no reason why it should be lowered simply because the currency authorities have been facing temporary difficulties. If, on the other hand, the contrary is proved, and the ratio is not held to be justified by the known criteria of internal and external monetary equilibrium, if, for example, the rupee has been like sterling which was overvalued in relation to the dollar until recently and had threatened the balance of payments of Great Britain and was, therefore, allowed to depreciate to reach a natural level, then, of course, there is a rational case for devaluation.

RESOLUTION OF THE CONGRESS WORKING COMMITTEE

There is no doubt that the Working Committee of the Congress did not state the real issues clearly in the resolution which was the subject of a recent Government *communiqué*. They say, "Since June last the balance of trade has turned more and more against India. The Committee are of opinion that the rate of 1*s*. 6*d*. to the rupee has hit hard the agriculturist of this country by lowering the price of agricultural commodities and given an undue and unfair advantage to imports into this country. The Working Committee is satisfied that the rate of 1*s*. 6*d*. cannot any longer be maintained on the balance of trade." Unfortunately the Working Committee have started with a presumption which is not supported by facts analysed above. The Government of India seem to have made much of this error, but it is nothing but short-sighted complacency to regard the improvement in the active balance of trade since June, 1938, as signifying a real upturn of the trade cycle. In fact, as the Monthly Review of Business Conditions in India during October shows, the foreign trade position

deteriorated and the larger exports of gold maintained the balance of payments as a whole. The second of the three statements quoted above, coming as it does after the first (which, as a statement of fact, is erroneous), obviously appears to be connected with the first, and since it refers to a mistaken view of the situation as it developed after June, 1938, it loses its force as an argument. The reply of the Government of India that "Since June last the trend of the price-index of the chief articles of export has been definitely upwards" seems to clinch the argument, although there is little evidence to be unduly optimistic about the trend of prices of primary commodities such as India exports. But from a broader point of view it is a truism that India has suffered after 1931 from a heavy price deflation which has been without precedent in the rest of the sterling bloc, Indian agriculturists have been hit hard both absolutely and relatively, and since, owing to gold exports, the balance of trade could not be readjusted to a lower level of imports, foreign imports have been restricted to a much smaller extent than they would have been otherwise. The Working Committee further say that during the last seven years the rupee ratio "has been maintained by large exports of gold which have been very injurious to the country." It is true, as we have already explained, that gold exports have fortuitously helped the currency authorities to maintain foreign exchange on an even keel; but we do not maintain that gold exports *per se* have led to economic disaster. What we condemn is the fundamental cause of such gold exports, *viz.*, the grinding price deflation which has made the rupee as intolerable as gold currencies. The Working Committee have also expressed their apprehension that "sterling resources have already been used up to an alarming extent, and there is a danger of further serious depletion taking place if efforts continue to be made by the Government of India to maintain the present ratio." If we examine thoroughly how far inroads have been made upon the sterling securities of the Issue Department of the Reserve Bank, it would appear that the ratio of "A" to liabilities in the Issue Department is still

about 9½ per cent above the statutory minimum of 40 per cent. Hence, the extent to which sterling securities of the Issue Department may be drawn upon without deflationary effect on the note-issue is not inconsiderable. In extreme emergency a part of the gold held as an asset of the Issue Department may also be utilised with safety, because the total value of the gold held in the Issue Department was Rs. 44 crores and about 41½ lakhs on December 16, 1938, whereas the statutory minimum is Rs. 40 crores. It appears, therefore, that although there is no need for "alarm" at the moment, yet since the depletion of sterling securities has been still continuing there is obviously no ground for self-complacency either. The Working Committee further argue that "Matters have now reached a stage when the rate can only be maintained by a policy of contraction of currency and credit." A careful analysis will show that during the period April to July, 1938, there was phenomenal contraction of notes in circulation and that it is not unreasonable to think that there was considerable active deflation, although the contraction of the note-issue was obviated to some extent by the lowering of the ratio of "A" to liabilities in the Issue Department. So far as credit is concerned the Reserve Bank followed during this period a commendable policy of easy money in relation to the short-term capital market. During the second half of 1938 there was a gradual expansion of notes in circulation, but the abnormal rise in the yield on Treasury Bills and heavy sales of these Bills created "unseasonal stringency" in September, and later on the monetary stringency which developed must have strengthened the basis of the rupee-sterling exchange.

GOVERNMENT COMMUNIQUÉ ON THE RUPEE RATIO

It is interesting to estimate the probable effects of devaluation according to the *communiqué* of the Government of India. "The Government of India are convinced that a lowering of the ratio in the existing international market conditions would produce no appreciable rise in what the cultivator

can realise for his produce. They are equally convinced that it would produce an immediate rise in the cost of what he buys." It is said that there will be no *appreciable* rise in export prices as the result of devaluation. Having maintained that our export prices are on the up-grade they cannot but admit that there would be a bounty on exports to the extent of the depreciation immediately. The bounty may not be appreciable but is certainly welcome in view of the collapse of export prices since the spring of 1937. But even if the up-turn in the cycle of prices and business activity fails to materialise in the immediate future, as we have reasons to think it will, devaluation would still be an effective instrument for fighting the economic relapse. In this connection we are strongly reminded of what happened in the case of Australia when she allowed her pound to depreciate 50 per cent on gold and 20 per cent on sterling in order to fight the depression. As Professor Copland observes, "With the depreciation of the currency the fall in export prices in Australian currency stopped, though there were minor fluctuations."[1] In January, 1931, the export price index number was 51 per cent of the 1928 level in Australian currency. It fluctuated around 55 per cent until the middle of 1933, and rose to 72 per cent of the 1928 level in the year 1933–34 as the result of a strong rise in wool prices. On the other hand, prices in terms of gold reached a desperate position of 30 per cent of the 1928 level by the beginning of 1933. This was certainly no mean achievement, and the statistics show that the volume of Australian exports was not only maintained but even increased through favourable seasons. India should certainly consider herself fortunate if she could at least prevent export prices quoted in rupees from falling by devaluating her currency. In the second place, the Government of India in their natural solicitude for the peasantry who form the backbone of our economic life, fear that devaluation would be ill-advised since it would *immediately* increase the cost of imported goods that the peasant buys. Theoretically,

[1] *Lessons of Monetary Experience*, the paper on "Australian Monetary Policy in Depression," p. 410.

devaluation operates as an *ad valorem* restrictive duty on imports at the same time as it acts as a bounty on exports. But it is a fallacy to think only in terms of the short-period effects of devaluation and to suppose that all the effects are exhausted in the short period. As we have said above, "There is a permanent advantage in foreign trade to the extent that certain internal costs, such as long-term interest and rent charges (and to a smaller extent various tax charges) which form important elements of cost in Indian agriculture and are fixed in terms of money, fail to rise. Moreover, even supposing that most of the direct advantage of depreciation is temporary, since currency depreciation in a period of depression has that kind of expansionary and recuperative effect upon internal economy which is cumulative in its momentum, it has ultimately an expansionary effect upon both exports and imports in the long period." Let us suppose for the sake of the argument that the prices of imported and other goods rise eventually as the result of devaluation which is accompanied by internal price reflation. Now since the cultivator will enjoy a temporary bounty on exports and also a certain permanent advantage in foreign trade, his spending power will increase and he will afford to pay higher prices for the industrial products that he buys. For example, in Australia after devaluation had been achieved imports increased from £44 millions to £56·6 millions during 1932–33 and rose to £82 millions by 1935–36. In the words of Professor Copland, "*Imports were recovering with the increased spending power accompanying recovery,*"[1] and at the same time the remarkable recovery of the export trade "obviated the necessity for incurring new borrowings in London."[2] Moreover it is necessary to bear in mind that when devaluation is accompanied by suitable, well-planned measures to initiate and speed up economic recovery (which are briefly discussed below) the prices of goods consumed by the masses need not necessarily be high in the long run. In Australia, for example, "the careful attention given to export production so that it might expand and the fostering of efficient secondary production

[1] *Lessons of Monetary Experience*, p. 419. [2] Fisher, *Stabilised Money*, p. 340.

competing with imports, were integral parts of the policy of recovery."[1] Similarly, speaking of Japan, Mr. Eigo Fukai says, "we have also been favoured by a high productive capacity. If production could not keep pace with the increase in consumers' demand stimulated by the injection of increased supplies of money, a rise in prices would certainly result. So as long as there is a high potential productive capacity the supply of goods may be increased and high prices will not necessarily follow, but only augmented production and expansion in business transactions."[2] It is not necessary to assume that the "potential productive capacity" of India will not rise to the occasion if devaluation is accompanied by a rational plan of recovery and industrial expansion.

Another argument which has been used by the Government against devaluation is that "It would seriously weaken the budgetary position of the Central Government and the larger Provincial Governments." Payments made overseas by the Central and Provincial Government include interest on sterling debt, leave salaries and pensions, apart from the cost of stores. The total involved is about £35 million and in the event of devaluation these transactions alone would add another Rs. 5 crores to Indian Central and Provincial expenditure. As to India's general annual purchases from overseas, if the rupee ratio was lowered to 1*s.* 4*d.*, Rs., 120 crores would have to be spent on what we are purchasing to-day for Rs. 105 crores. It is unfortunate that the Government of India fail to recognise the expansionary effects of devaluation on exports as well as imports and on the entire internal economy. After all, the Government budget reflects the state of economic activity and is dependent upon the incomes and profits of the people. If there is an all-round increase of both money incomes and real incomes, if there is increased turn-over of goods and business activity, and if both internal and foreign trade are stimulated as the result of devaluation and allied measures of economic recovery, there is every reason to believe that the loss

[1] Copland, "Australian Monetary Policy in Depression," p. 421.
[2] *Lessons of Monetary Experience*, p. 394.

sustained by way of exchange premium on our foreign debt services would be more than made good by the increasing yield of the different sources of taxation. In the case of Japan the statistical evidence indicates that as the result of the depreciation of yen there was "an increase of some 30 per cent in the people's savings accumulated in the various financial institutions, a 50 per cent increase in the output of staple manufactures, the doubling of the value of exports, and a gain of some 40 per cent each in the national railway freight traffic, bank clearings and factory employment."[1] It cannot be seriously suggested that such amazing recovery of economic activity and rise of incomes, profits, savings, investment and employment did not react favourably upon the Government budget. Similarly in the case of New Zealand[2] "The effect of the depreciated exchange has been to raise export receipts in terms of New Zealand currency. For the latest year export values are about £ NZ 50 million. At par of exchange with sterling they would have been £ NZ 40 million. The direct result is, therefore, to increase receipt from overseas, to expand the national income and the spending power of the people, to promote more active business, to maintain all security values and to augment taxable capacity. The only important money cost to the budget is the exchange premium on the debt service overseas which amounts to about £ NZ 1.75 million on annual payment approximating £7 million sterling. On the other hand the increase of £ NZ 10 million in export receipts circulates throughout the country, stimulates all other industries, and tends to be more than doubled in its effect upon the national income. The gain in revenue from taxation, which ranges from 20 to 25 per cent of the national income, tends, therefore, to be much greater than the cost of the exchange premium to the budget." In the same manner in Australia the rise in the index of Ordinary shares from a low of 52·1 in January, 1931, to 86·5 in July, 1933, and of Preferred shares from

[1] *Lessons of Monetary Experience*, p. 394.

[2] Mr. A. H. Tocker in *Economic Record*, March, 1935, p. 90, quoted by Dr. B. P. Adarkar in *Indian Finance*, August 6, 1938.

80·8 to 106·9 in the same period and the rise in the price of Government securities in spite of the drastic reduction of yield, indicated rising business activity which meant increased taxable capacity all round.

RE-ORIENTATION OF MONETARY AND FISCAL POLICIES

In the concluding portion of this essay we shall make an attempt to indicate the general lines on which there should be a re-orientation of the monetary and the fiscal policies of the Government if devaluation is to produce enduring results by initiating and speeding up the process of economic recovery. Monetary policy is not the be-all and end-all of economic policy. It is nothing but an aid, and sometimes an indispensable aid, to sound economic policy. Our economic policy must necessarily be broad-based on the fundamental objective of correcting the distortions in the structure of prices and production created by the Depression. To reach this goal we require a co-ordinated programme in which both monetary and non-monetary measures must be combined and assimilated.

An economic depression which is a process of deflationary contraction always means a tremendous loss of real income. It is possible by monetary measures to keep the loss of national income in terms of money as low as possible. But the most pressing economic problem which arises in the course of depression is that the loss of real income is not *quickly* and *evenly* distributed over all classes of the community. Deflation attacks certain incomes only and thus increases the disparity in real incomes amongst the different economic classes. Thus falling prices, in the absence of expansion of total productivity, automatically increase the share of the national income going to that section of the community which has fixed money claims. This rigidity of the debt structure based on contractual money claims is one cause of the unequal distribution of the loss of real income and of the distortion of the structure of production. Another cause is the rigidity of the cost structure. A rigid debt structure helps to create a rigid

cost structure. But in the case of the industrial employer there are many other rigid items; at least half of his costs of production is normally represented by such rigid items, including, notably, wages. Wage reductions are not possible because rent and a number of other items comprised in the cost of living do not move in harmony with wholesale prices. As Sir Henry Strakosch has pointed out, in the post-war world a peculiar rigidity has been imported into the cost structure for reasons which he summarises as follows: "(*a*) Increased division of labour, with its corollary of increased overhead and relatively static charges; (*b*) increased mechanisation coupled with larger individual units of production (again involving a greater ratio of fixed overhead charges); (*c*) an increased proportion of the world's economic activity devoted to services—*i.e.*, distribution and selling—whose costs do not react rapidly to a fall in wholesale prices; (*d*) increased use of credit (whose costs also are 'sheltered') in the process of production; (*e*) increased cartelisation of industry, with the inevitable consequence that finished prices tend to move less sensitively than prices of 'unsheltered' primary products."[1] In a predominantly agricultural country (in which a vast mass of indebtedness hangs like a mill-stone round the neck of the peasantry) the disturbance in the costs-prices equilibrium is likely to be more serious as the prices of "unsheltered" primary products are particularly sensitive. Hence the outstanding evil of the prolonged process of deflation to which India has been subjected has been the unequal and slow distribution of the loss of real income caused by the economic crisis and a corresponding distortion of the structure of production. Any measure by which we can distribute the loss of real income quickly and equitably amongst all classes other than the agriculturists will be a step towards economic recovery. It will lower the cost of agricultural production, increase the volume of goods that the agriculturists could buy from domestic industry, reduce unemployment, increase the margin between revenue and expenditure in the Central and Provincial budgets,

[1] *Lessons of Monetary Experience*, p. 175.

increase the volume of domestic production competing with imports and help to restore our trade balance to a sound and stable basis.

ALTERNATIVE REMEDIES

There are several ways of restoring the costs-prices equilibrium and shifting a part of the inequitable burden of loss of real income which rests on the producers of primary products to other sections of the community. There are some who believe that the equilibrium should be restored by an automatic lowering of costs in the *long run*, and when this happens eventually the loss of real income will have been evenly distributed over the community. But they forget that leaving things to nature makes the process of economic adjustment slow and painful to the point of desperation. As Sir Henry Strakosch has explained, a peculiar rigidity has been imported into the cost structure in the post-war world. The costs-prices equilibrium encounters nowadays almost irresistible economic friction, and natural forces are powerless to restore this equilibrium in a great majority of cases. Moreover, the problem assumes a serious aspect in the case of a country like India, where the disequilibrium is so violent owing to the high sensitiveness of the "unsheltered" prices of primary products, where there is a vast mass of agricultural indebtedness, and where the agriculturists who have borne the brunt of the crisis are least able to bear it. "A primary producing country with a heavy proportion of fixed interest-bearing debt cannot enter lightly into a course that will cut in half the prices of its leading products. The debt problem is much too difficult of adjustment on this basis without serious financial disturbance."[1] It is quite evident that the painful process of deflation has driven the Indian peasantry to a point of desperation. Compulsory scaling down of debts and the abatement and arrears of land revenue demand in all parts of India have been tried as remedies, but they have proved to be desperate palliatives

[1] Copland, *Lessons of Monetary Experience*, p. 414.

which tend to cure only the symptoms of a deep-rooted economic malady which has reached a critical stage. Compulsory debt settlement of the kind attempted in the various Provinces of India is a method of debt adjustment which has not been free from "serious financial disturbance" in the countryside. It has had a tendency to retard economic recovery, and by scaring creditors has very often worked ultimately against the interests of the agricultural debtors, while it has fanned the smouldering fires of class conflict. Abatement and arrears of land revenue demand are also temporary palliatives and cannot really go very far without threatening budgetary equilibrium and accentuating the class conflict. Moreover there is a danger that the Provincial Governments may develop a deflationist mentality. In times of acute economic depression "tendencies to level up incomes which are more often based on vague sentiment than on calm consideration are combined with the puritanical wave. Almost every country, it seems, has at some time during the last depression gone through a period of being plagued by this puritan bad conscience about 'too much spending' and the cry for a 'drastic reduction of expenditure all round.' In Germany the atmosphere was thick with it during the chancellorship of Brüning and the British Economy Stunt of 1931–32 seems to have amounted to the same thing."[1] But the fact is that we are living in poverty in the midst of plenty, and economic recovery being nothing but a process of getting rid of surplus goods and surplus productive capacity, reduction of consumption and ultimately the measures which bring about a reduction of consumption can never be a way out of the impasse. One should not deny that a deflationary process has a purging effect, and a certain amount of deflation is perhaps necessary for the restoration of economic balance. Speaking of Japan, Mr. Fukai observes that "The productive capacity of the nation was improved during the period of depression making available a supply of goods at less cost." But Japan, unlike India, did not allow the slow paralysis of economic activity to creep in, and hence,

[1] Röpke, *Crises and Cycles*, p. 182.

as he says, "when under the stimulus of low exchange and cheap money occasion arose for the advance of our goods to foreign markets, we were fully prepared to make the most of it."[1]

Another method of redistributing the loss of real income caused by the depression is to raise the real income of peasants by a compensatory adjustment of the tax structure. This is being attempted by Congress and non-Congress Governments in the Provinces. The section of the community which comprises the fixed interest rentiers, most salary earners, a large proportion of the skilled and upper-grade wage earners and the landlords usually experiences an increase in real income during the period of depression, and hence their taxable capacity rises. Hence a transfer of real income from these classes to the agricultural masses is being brought about by taxing the former more heavily or by otherwise reducing their real income (through retrenchment, salary cuts and reduced Government expenditure incurred on these classes) and by diverting the resources so obtained to social expenditure benefiting the masses, particularly to providing relief in the shape of reduction of land revenue. The same object can be still better achieved if the Central Government also introduce salary cuts and economise their expenditure, steepen the graduation of the income-tax at the higher ranges, introduce Death Duties and readjust their tax structure in co-ordination with the Provinces on the basis of a long-run trade-cycle policy. Such an economic policy will certainly secure distributive justice and give a much-needed immediate relief to the agricultural masses. But it is at best a palliative and cannot go very far without increasing the burden on economic enterprise, creating class conflict and disorganisation, and disturbing social and industrial relations. The repercussions of these on our economic life may be disastrous, particularly at a time when we are looking forward to economic recovery. What we should aim at is economic expansion and not more redistribution of the loss

[1] Eigo Fukai, "The Recent Monetary Policy of Japan," *Lessons of Monetary Experience*, p. 393.

of real income which is being attempted by the Provinces at the present moment. And for this purpose monetary policy is indispensable to a sound economic policy.

Another method which has found favour with some is to correct the costs-prices disequilibrium by restricting the supply of commodities, and particularly that of agricultural commodities of which there is supposed to be a serious glut. As Keynes says, "It may well benefit the producers of a particular article to combine to restrict its output. Equally well it may benefit a particular country, though at the expense of the rest of the world, to restrict the supply of a commodity which it is in a position to control. It may even, very occasionally, benefit the world as a whole to organise the restriction of output of a particular commodity, the supply of which is seriously out of balance with the supply of other things."[1] Schemes of crop restriction have been recently very popular in agricultural countries, and even international organisations have been set up to control and restrict the supply of essential raw materials and primary products on the basis of quotas. In India tea restriction and jute restriction are instances in point. In the cement and sugar industries the control of a sheltered home market behind the tariff wall has also led to regulation of supply in the face of sagging prices. But obviously in the sphere of agricultural production a restrictionist policy would require an elaborate and expensive machinery of restriction and usually succeeds in the case of crops produced on the basis of a plantation system of proprietary agriculture. But apart from the practicability of restriction schemes, "As an all-round remedy," as Keynes observes, "restriction is worse than useless. For the community as a whole it reduces demand, by destroying the income of the retrenched producers, just as much as it reduces supply. So far from being a means to diminish unemployment, it is rather a method of distributing more evenly what unemployment there is, at the cost of somewhat increasing it."[2] The Columbia University Commission in their report on Economic

[1] *Means to Prosperity*, p. 17. [2] Ibid., p. 17.

Reconstruction indicate the ultimate effect of restriction very incisively when they say that "an all-round application of this policy would make for general impoverishment and would solve the problem of 'poverty in the midst of plenty' by removing the plenty."[1] And we are inclined to agree with them when they further say that "Deliberate limitation of production and even physical destruction of goods and crops in order to raise the price of the remainder are in effect a confession of failure in respect of our present ability to deal with the major problem."[2]

PROGRAMME OF MONETARY REFORM AS AN AID TO ECONOMIC EXPANSION

It is clear then that the immediate objective of our national economic policy must be economic expansion. But as the first step towards it there must be a frontal attack at the monetary end. The rupee must be immediately devaluated in order to raise our export prices in terms of rupees at least to the level of April, 1936, the objective of devaluation being the restoration of the equilibrium between the cost structure and the price structure by quickly raising the export prices in terms of rupees. The Reserve Bank should at once give up the attempt of maintaining the present ratio and cease to make inroads upon the sterling assets of the Issue Department. On the other hand, if necessary it should start purchasing gold and sterling in sufficient quantities so as to reach and maintain the depreciated level of exchange decided upon as a measure of devaluation and to minimise the effects of foreign exchange fluctuations. For some time in order to check speculation it must retain its deflationary grip upon the money market and desist from active expansion of currency and credit. That such a course of action is necessary is borne out by the monetary experience of Sweden, Great Britain and Australia. The immediate

[1] *Report of the Columbia University Commission*, Columbia University Press, 1934, p. 38.
[2] Ibid., p. 12.

impact of exchange devaluation will be upon the international price level expressed in terms of rupees which will rise at once and almost in proportion to the extent of depreciation. Gradually the domestic price level will rise somewhat to the extent that the impetus of devaluation and the consequent expansion of purchasing power diffuse themselves through the economic system and affect that price level by an indirect process. But after a stage there must come stimulation of loan expenditure which Keynes regards as the means to prosperity. The first necessity, according to him, is "that bank-credit should be cheap and abundant. This is only possible if each Central Bank is freed from anxiety by feeling itself to possess adequate reserves of international money."[1] The Reserve Bank has no doubt lost a considerable amount of its sterling assets in the Issue Department, but still the ratio of "A" to Liabilities in the Issue Department is about 10 per cent above the legal minimum, so that there is still considerable scope for expansion of note-issue. As Keynes suggests, even "The abatement of the legal proportion of international money" (gold and sterling securities in the case of India) which the Reserve Bank must hold against its note-issue "might also help on a minor scale."[2] Moreover, since devaluation will mean an immediate appreciation of the value of gold and sterling securities in terms of rupees, the scope for expansion of note-issue will, to that extent, be widened. Thus, on the whole, it will be necessary and possible for the Reserve Bank to bring about an increase in the amount of notes in circulation and in the amount held in the Banking Department to facilitate loan expenditure. Purchase of securities and a lowering of the Bank Rate to 2 per cent (as was done in England in June, 1932) will also perhaps be necessary as supplementary measures. All these and other allied measures of real credit expansion are absolutely necessary if devaluation is to succeed, otherwise a dangerous reaction is bound to occur sooner or later, as it occurred in the

[1] *Means to Prosperity*, p. 20.
[2] Ibid., p. 20.

United States during the first year of the New Deal until a real expansion of credit was started.[1]

As Keynes says, provision of ample short-term bank credit is just the first stage in the programme of recovery. We explained above that, when there is still disequilibrium between the cost structure and the price structure, an easy money policy fails to have an expansionary effect. Liquidity preference being high in the case of long-term loans necessary for economic expansion, a large differential appears between the long-term rate of interest and the short-term money-rate. Hence the low short-term money rates serve an expansionary purpose only when long-term capital can be obtained on easy terms and there is increased demand for short-term credit to replace the working capital. As Keynes suggests, "A combination of manœuvres by the Government and the Central Bank in the shape of open-market operations by the Bank" is expected to lower the long-term rate of interest for reasonably sound borrowers.[2] Something of this kind will be necessary in India if economic expansion is to gather momentum.

Keynes is of the opinion that economic expansion cannot be financed out of current income which has fallen too low. The increased spending power which is to initiate and speed up the process of expansion must come out of loan expenditure on a large scale. Compensatory credit expansion, which draws upon unused productive reserves corresponding to the deficit of purchasing power created by deflation, is certainly a source of loan-expenditure. But Keynes thinks that the first step in initiating loan expenditure "has to be taken on the initiative of public authority; and it probably has to be on a large scale and organised with determination if it is to be sufficient to break the vicious circle."[3] This brings us to the public works policy as a means of fighting depression. The general principle involved in this policy is that the process of credit expansion should start with the State as the pioneer in starting new borrowing instead of the nervous and hesitant

[1] Röpke, *Crises and Cycles*, p. 190. [2] *Means to Prosperity*, p. 21.
[3] Ibid., p. 22.

entrepreneurs. Once the principle is accepted the rest is a question of technical detail. Already the Provinces have been evolving their reconstruction programmes requiring public works and projects of a productive character. There is thus a vast amount of productive expenditure that is waiting to be incurred on a nation-wide scale. Let this expenditure be loan-expenditure on a large-scale and, in the words of Keynes, "organised with determination." For this purpose we must have an All-India Loans Council, like the Australian Loans Council, which will co-ordinate the loan issues and determine their order and timing in such a way as to prevent too many competitive loan issues at a time and avoid a rise in the terms on which credit can be obtained. The best policy is to tap the short-term capital market by selling Treasury Bills, because the short-term money rates at the moment are lower than the long-term rates and are likely to be so at the initial stage. This may be financial unorthodoxy but is certainly the most rational way of financing loan expenditure for fighting a depression. But the Reserve Bank will have to thoroughly revise its policy regarding the sale of Treasury Bills on behalf of the Provincial Governments. It must itself purchase these Bills as part of its policy of credit expansion and thus enable the Provincial Governments to borrow money for economic expansion on reasonably low terms, and must determine the order and timing of the Treasury Bill tenders on a rational and co-ordinated plan in consultation with the proposed All-India Loans Council.

CHAPTER XXIX

THE STRUCTURE OF INDIAN BANKING

By The Late Sir S. N. Pochkhanawala

Early History

Landmarks in the history of Indian banking.—A bird's-eye view of the landmarks in the history of Indian banking will, at the outset, be helpful in providing a correct perspective for an examination of the Indian banking structure.

It is wellnigh impossible to fix a definite date marking the origin of banking in India. As Cooke remarks in his book on *Banking in India*, "it is not improbable that long before England had ranked in the scale of nations, India had adopted a system of banking which may have originated that now in use with the Shroffs or native bankers." Researches by scholars have brought to light both literary and epigraphical evidence showing the hoary antiquity of Indian banking. The laws of Manu and the "Arthashastra" of Kautilya abound in references to the banking practices of those remote ages. Coming to later times we find that during the Moghul period the indigenous bankers wielded enormous political power at the Royal Court. In addition to lending freely and frequently to the Royal treasuries in times of national emergency, these native bankers, who came to be known by a variety of names in the different parts of the country, engaged themselves in trading on their own account. Their business was usually hereditary, with the result that, on account of the incapacity of their successors, many of these houses suffered.

For the first few years after the advent of the East India Company they retained their former position of importance

by undertaking the collection and transmission of revenue on behalf of the Company, but, as a result of the gradual establishment of Agency Houses by the European traders themselves, the indigenous bankers were, in course of time, shorn of much of their glory.

A financial crisis, perhaps the first of its kind, occurred in 1830–32 and proved disastrous to the Agency Houses themselves, though it indirectly helped the further growth of the Government Savings Institutions which had been started in 1810. Between 1800 and 1858, more than 40 new banks were established, but hardly 12 of them survived, the most important among the latter being the three Presidency Banks of Bengal, Bombay and Madras, which had come into being in 1806, 1840 and 1843, respectively. These Presidency Banks functioned as Government bankers, enjoying even the much-coveted right of note-issue till 1862, in which year that privilege was concurrently withdrawn. In January, 1921, they were eventually amalgamated as the Imperial Bank of India.

The speculative mania which raged between 1864 and 1866 brought about the establishment of a large number of mushroom banks; but history repeated itself shortly afterwards, and most of them had to close down with heavy losses. The first decade of the present century, on account of enthusiasm for Indian enterprises arising out of the partition of Bengal, gave a good deal of stimulus to the formation of Indian Joint-Stock Banks; but unfortunately the crisis of 1913–14, probably the worst in India's banking history, seriously interfered with their growth. It left few of them unscathed, and most of them came to grief. Gradually, however, the spread of the Swadeshi movement helped in a general resurrection and the more important of the banks flourishing to-day were able to consolidate their position. Along with the indigenous banks, the number of foreign banks operating in India also showed an increase. From the very beginning the latter took to exchange business, which still remains practically their monopoly.

The absence of a Central Institution to co-ordinate the

activities of these diverse elements had long been keenly felt, and, after years of discussion and agitation from the time of the Chamberlain Commission onwards, it was sought to be remedied in 1927 when the late Sir Basil Blackett introduced his Reserve Bank Bill. The proposal, however, for a Shareholders' Bank as adumbrated in the Bill raised such a storm of protest in the Legislature that, between the Scylla of unrelenting non-official opposition on the one side and the Charybdis of Government's firm attitude on the other, the Bill tottered for some time and ultimately foundered. Things drifted on till the elaborate banking enquiry instituted in 1929 once more brought the question to the forefront. Meanwhile, the embers of political controversy aroused by the previous ill-fated Bill had died out, and this fact, coupled with the insistence of the British delegates to the Round Table Conference that the creation of a Reserve Bank should be a condition precedent to the transference of power to Indian hands, impelled the Government of India to come forward with fresh legislative proposals. The new Reserve Bank Bill was eventually passed into law in 1934, and from April 1 of 1935 the Reserve Bank of India commenced regular work, thus fulfilling at last the hopes which had been cherished for many a decade and which at times had appeared almost beyond fruition.

The Reserve Bank of India

Its national responsibilities.—With the inauguration of the Reserve Bank of India, a new and important chapter in the history of Indian banking has commenced. It is an event fraught with momentous consequences for the future of Indian banking institutions and for India's financial autonomy. The potentialities for fostering the growth of banking in India have been enhanced by the creation of the Reserve Bank, and it is to be hoped that by judicious guidance and the exercise of wholesome influence the Reserve Bank will establish the banking structure of the country on a sounder foundation than the one it possesses at present.

The banking edifice, as it stands to-day, comprises the Reserve Bank of India (as the apex bank), the Imperial Bank, the Exchange Banks, the Indian Joint-Stock Banks, the large body of indigenous bankers who are known by a variety of names in different parts of the country, and, lastly, the Co-operative Banks.

The Reserve Bank forms the keystone of the arch and occupies a unique position as the country's Central Bank. It possesses many of the privileges and responsibilities of Central Banks in other countries, and is in a position to play a predominant part in moulding the future of Indian banking. The development of Indian banking in general is a necessary preliminary to the attainment of financial self-sufficiency, and hence it is impossible to exaggerate the importance of inculcating in the mind of the average intelligent layman a critical but at the same time sympathetic interest in matters germane to that ideal. Let us, therefore, consider briefly how the Reserve Bank can fulfil its laudable mission of fostering the all-round economic prosperity of the country.

The responsibilities attaching to the exalted position that the Reserve Bank occupies at the head of the banking structure are no less great than the prestige that it is rightly endowed with. It is, as it were, the arbiter of the nation's destinies in the banking world, and it is, therefore, essential that it should, at all costs, hold the scales even as between the various classes of banks that come under its sway, and dispense justice without fear or favour. In no event should it seek to placate the vested interests of one group to the detriment of another.

Further, the Reserve Bank should recognise that the conditions obtaining in India are of a peculiar character not met with elsewhere in the world, and that they therefore demand special treatment. In particular it should be the first charge of the Reserve Bank to create a congenial atmosphere for the progress of indigenous banks and engender in them a sense of security. Taking advantage of the absence of co-ordination and control from a common authority, the foreign banks have been able to flout national

aspirations, and this factor has been eating like a canker into the very vitals of the Indian banks and has been stifling their healthy growth. If the indigenous banks whose record of service is unimpeachable are to launch forth into wider seas instead of drifting helplessly along in the stagnant backwaters as at present, they should, in the first place, steer clear of the rock of foreign competition, and for this purpose they need the piloting skill of the Reserve Bank. Even if discriminatory legislation against the non-indigenous banks is not considered desirable, it should at any rate still be possible for the Reserve Bank to make a sustained effort to keep the latter within bounds. In this connection, it is a matter for regret that the suggestion made by witness after witness before the Central Banking Enquiry Committee to the effect that no foreign bank should be allowed to operate in India without obtaining a licence and that the Government should exercise adequate control over foreign institutions, has been brushed aside. No such provisions have been embodied in the Reserve Bank Act, and the result of this unfortunate omission is that the non-indigenous banks, with large resources and vast experience at their back, will continue to have the field to themselves without let or hindrance. Unless the Reserve Bank is armed with the necessary powers to put a stop to the unfair competition of non-indigenous banks, the future of the indigenous institutions cannot but be gloomy. Again, unless the Reserve Bank is in a position to exercise the same measure of effective control over indigenous and non-indigenous banks alike so as to prevent them from flying at each other's throats, and thereby spoiling the chances of profit to either, it cannot function as a Central Bank in the true sense of the term. Active assistance to indigenous banks in a variety of ways should, in short, be the touch-stone of the Reserve Bank's success as a national institution.

Nor should the indigenous banks be content with resting passively on their oars. The serious set-backs suffered by them in the past were due in a large measure to the lack of unity among themselves, and this the foreign banks

were not slow to exploit. Without the development of mutual goodwill and solidarity among the Indian banks themselves, any attempt made by the Reserve Bank towards the amelioration of their condition is doomed to fail in its purpose.

Under the Reserve Bank of India Act (1934), certain banks having a paid-up capital and reserves of an aggregate value of not less than Rs. 5 lakhs are allowed the privilege of being placed by the Governor-General in Council on the list of Scheduled Banks. These banks are required, under the Act, to comply with certain requisitions, the principal of these being a compulsory deposit with the Reserve Bank of not less than 5 per cent of their demand liabilities and of not less than 2 per cent of their time liabilities. This requisition of a compulsory deposit although it practically implies nothing so far as the stability of the bank is concerned, has promoted in the mind of the general public the belief that the mere fact of a bank having been placed on the list of Scheduled Banks is in itself an indication of its strength and safety. This impression, on the face of it, is erroneous, and if the Scheduled Banks were prohibited from giving publicity through their advertisements or through any other medium to the fact of their being such, the erroneous impression would not gather strength and would, in course of time, die out.

It might, incidentally, be mentioned that there prevails a worse practice amongst certain banking institutions of giving undue publicity to the figures of their authorised capital, when their paid-up capital is but small and compares unfavourably with the former. This practice, inasmuch as it is apt to mislead the public, is reprehensible and should certainly be discouraged.

The efficiency of a banking system depends ultimately upon its stability, adaptability and initiative; and it is by this threefold crucial test that the Reserve Bank will be eventually judged before the bar of enlightened public opinion. In all that it does, the Reserve Bank should pursue a "bold, active, forceful, and energetic policy." The promotion of Indian interests above everything else should

be its sole concern. Let us hope that it would so shape its policies and activities that when the time arrives for appraising the worth of its service, it would be unanimously acclaimed as a great institution that brought about the transformation of the Indian banking system into a well-designed instrument for the furtherance of national well-being.

The Imperial Bank of India

Supreme importance of co-operation between the Imperial Bank and joint-stock banks.—The Imperial Bank of India came into being on January 27, 1921, as a result of the amalgamation of the three Presidency Banks. The total of its paid-up capital and reserve on that date amounted to Rs. 9·37 crores, and rose to Rs. 11·05 crores as on June 30, 1935. It inherited the privileges and restrictions of its predecessors with some minor modifications and continued to function till the recent establishment of the Reserve Bank as the State Bank doing treasury work and enjoying the use of interest-free deposits from Government and from various other public bodies. It was not a Central Bank in the strict sense, since it lacked the one essential attribute of Central Banks, namely, the right of note-issue. Whatever influence it sought to exercise on the money market by determining the Bank Rate was neutralised to a large extent by the exigencies of Government finance and, as a result of this lack of autonomy, it failed to have any effective voice in shaping either the currency or credit policy of the country. As the late Sir Basil Blackett vividly described it, it was at best only "a hybrid institution trying painfully to combine incompatible functions." It has always remained in essence a purely commercial bank, and, through its network of about 200 branches and pay-offices spread over the whole country, it has been rendering good help in financing its internal trade. In fact, it was the fear that the conversion of the Imperial Bank itself into the Reserve Bank would involve the serious loss to the community of the benefit of this elaborate and wide-spread organisation that was mainly responsible for the decision in favour of

creating a distinct and separate Reserve Bank for the country.

Owing to the advent of the Reserve Bank of India, the Imperial Bank has been deprived of some of its privileges. At the same time, many of the restrictions under which it had so far been labouring have been removed, leaving it free to enter the field of foreign exchange business. Thus, it stands to-day as the most powerful and important commercial bank in India, still commanding funds in excess of the combined resources of all the Indian Joint-Stock Banks. As the Hilton Young Commission observed in paragraph 90 of their Report, "the banking organisation which India requires must be based not upon a Central bank alone as elsewhere but upon a Central bank and a great commercial bank" to serve the needs of the scattered population. It is, therefore, all the more necessary that, in the interests of Indian banking in general, the long-standing rivalry between the Imperial Bank and the Indian Joint-Stock Banks is now ended and they co-operate and work together as helpful partners under the aegis of the common parent body, the Reserve Bank of India. The fact that, in the past, largely because of the commercial character of its activities, and the resultant clash of interests, the Imperial Bank often indulged in intensive competition with the indigenous banks in the financing of the internal trade, cannot be ignored. Now, however, that things have assumed a different shape through the establishment of the Reserve Bank, it behoves the Imperial Bank to join hands with big Indian banks to their mutual advantage and devise ways and means for furthering the wider cause of banking progress in the country by adopting the principle of "Live and let live."

It is desirable, in the cause of Indian banking, that the Imperial Bank should turn to exchange business, so that this business may not continue to remain the monopoly of the non-indigenous banks. It is true that there are still certain difficulties in the way of the Imperial Bank's taking up this branch of business, but if with such vast resources at its back it does not step in at an early opportunity, there

will hardly be any chance for any other Indian bank to succeed in this line. If the Imperial Bank, as the most prominent commercial bank in the country, were to take the lead in this matter and undertake exchange business on a large scale, the other Indian banks would be only too glad to render all possible assistance by transferring to it a large portion of their own exchange business.

The need for co-operation between the Imperial Bank and the Joint-Stock Banks which has always been great was never greater than to-day when it is entering upon a new era in banking business. It is the duty of the Imperial Bank to stop all unhealthy rivalry amongst Indian banks, and it should not make business impossible for the latter by quoting such rates for advances as would leave them hardly any margin of profit. There is one particular matter in which a beginning is both urgent and expedient. The Imperial Bank should take the lead in setting up an Association of Indian Banks on the analogy of the Exchange Banks' Association, with the avowed object of providing a united platform for the discussion and solution of banking problems of common interest. The formation of such an Association is long overdue and should be taken in hand without any further delay, for not only would that assist in bringing about better understanding and greater amity among the Indian banks themselves, but it would also serve as a weighty medium for ventilating their grievances. The views expressed by and the proposals emanating from such an organised body would command greater respect and attention, and Government and the Reserve Bank would, naturally, give their suggestions due consideration.

Exchange Banks

Dominating position of Exchange Banks.—The financing of the import and export trade of India has for a long time been monopolised by non-indigenous banks whose interests are more often than not diametrically opposed to the interests of the country. These institutions managed to obtain their foothold in this country prior to

the establishment of Indian Joint-Stock Banks who have been forced to remain in the background partly on account of this initial handicap. Their number has grown from 2 at the time of the transfer of India to the Crown to 18 at the present day. Originally these non-indigenous banks started their operations in India with the ostensible object of doing exchange business alone, but latterly they have entered the field of financing the internal trade as well, thus offering formidable competition to the indigenous banks. Again, while in the beginning they confined their activities to the principal ports of India, their tendency during the post-war period has been to extend their spheres of influence into the interior. Naturally, all this has resulted in unhealthy competition and rivalry with the indigenous banks who are left powerless to resist these inroads. Owing to the absence of a central controlling authority, these non-indigenous banks have been enjoying all this time unfettered freedom in their struggle with the Indian Joint-Stock Banks and have become a menace to the latter.

The rapidity with which the volume of their Indian deposits has been increasing is really alarming and emphasises the urgent and paramount need for safeguarding the interests of indigenous banking institutions. In 1913 their total deposits in India amounted to Rs. 31 crores, and they swelled to Rs. 74 crores in 1932. Perhaps a clearer idea of the extent of their competition can be gathered by a study of the following table which shows the proportion which their Indian deposits bear towards the grand total of bank deposits in the whole country.

	Imperial Bank		*Indian Joint-Stock Banks*		*Exchange Banks*	
Year	*Deposits in crores of Rs.*	*Percentage to total deposits*	*Deposits in crores of Rs.*	*Percentage to total deposits*	*Deposits in crores of Rs. (in India)*	*Percentage to total deposits*
1913	36·49	40	24·10	26	31·04	34
1923	74·20	39	47·69	25	68·44	36
1926	73·90	36	63·15	30	71·54	34
1929	71·64	35	66·30	32	66·66	33
1931	63·86	32	66·07	34	67·47	35

The question naturally assumes greater importance when we take into account the fact that, while the foreign trade of India bears only a small proportion to the huge volume of internal trade, the Exchange Banks enjoy a much larger share of the total available deposits of this country.

One possible explanation of this paradox lies in the age-long habit of the people of this country of crediting every institution that is of foreign origin as possessing greater stability than corresponding indigenous institutions. To a certain extent this readiness to place greater reliance in the soundness of foreign banks is due to the failures at periodic intervals of several indigenous banks. Alarmed by the recurrence of such failures the people have been prone to jump to the conclusion that indigenous banks cannot be as secure as their foreign rivals, but things have now improved considerably and the rapid growth of sound indigenous institutions even in the face of the heavy odds pitted against them is sufficient evidence that public distrust in them is fast disappearing.

While the Indian deposits of the Exchange Banks have been mounting up, the ratio of their Cash Reserves against their Liabilities has always remained alarmingly low. Pointed attention was drawn to this by J. M. Keynes, among others, who remarked that possibly the Exchange Banks had been in smooth waters longer than was for their good. Again, the Exchange Banks with their head offices abroad would, and in most cases do, look to London for assistance in times of difficulties; seldom do they seek the help of the Imperial Bank. Having ample resources at their command at their head offices and other branches, these banks are able to draw upon unemployed funds in times of need; the indigenous banks having no such support to fall back upon suffer in competition and find it difficult to flourish. "The foreign banks thus form an unabsorbable and uncontrollable part of the Indian banking system." This partly explains the strenuous opposition with which the Exchange Banks greeted all proposals for the unification of the banking structure of India. Apprehensive of losing their monopoly by the entry of the Imperial Bank into the field of exchange

business they opposed the very formation of the Reserve Bank and the resultant freedom of the Imperial Bank from the statutory restrictions regarding foreign exchange business. Instead of being willing and useful helpmates to the other members of the banking system they enter into rivalry sometimes bordering on cut-throat competition after having entrenched themselves in an impregnable position with the aid of their huge reserves and the cheap money they can command in their home countries, whose interests they naturally always have at heart. Their prime concern has been the development of the industries of their own countries, and this they achieve by financing the export of India's raw produce and the import of the finished goods of their own countries into India, and, mostly, they employ the funds obtained by them in India to promote the industrial pursuits of their own countries. Perhaps, if, as Sir Stanley Reed has pointed out in his evidence before the Hilton Young Commission (Vol. V, p. 246), they had been entrusted from the very beginning with the responsibility of settling the account relating to India's balance of trade instead of being "spoon-fed" by Government, they would have been inclined to fit in more readily into the banking machinery of the country.

The question of restricting the Exchange Banks' business.—Our "open-door" policy towards these Exchange Banks has not received from them the appreciation it deserves, and due, principally, to the formidable competition of these powerful rivals in various directions and due to lack of sympathy on the part of the authorities, Indian joint-stock banking has all along remained in the background. Unless steps are immediately taken to check this growing competition, the position of the Indian banks threatens to become precarious. This question of restricting the activities of the Exchange Banks was dealt with at length by the Indian Central Banking Enquiry Committee, which recommended in their majority report the adoption of the Japanese system of the issue of licences to foreign banks. Even this recommendation, however, which was mild compared to the more

drastic, but none the less necessary, restrictions suggested in the minority report, has not been acted upon so far. It is high time that a Bank Act is passed empowering, *inter alia*, the Reserve Bank to exercise control over these foreign banks and to restrict their operations to the principal port towns. It is also necessary to see that the foreign banks confine themselves to their legitimate business of financing the foreign trade, without encroaching on the sphere of indigenous banks.

It may be of interest at this stage to notice what steps other countries have taken to regulate and restrict the work of foreign banks operating within their boundaries. The Bank of England restricts the rediscounting and other facilities to banks of British origin alone, and foreign banks have to do without these facilities. In the United States of America foreign banks are not allowed at all to receive deposits within the country, and, in addition, the volume and the character of the business in which the foreign banks may be engaged is specifically defined and limited. Foreign banks desiring to open branches in Denmark are required to obtain previous permission from the Government, and they have also to abide by the undertaking that no non-Danish subject should be made the Manager of a branch in Denmark. France and Italy insist on the payment of an incorporation tax by foreign banks that wish to open branches, and, in addition, a turn-over tax is also levied on their exchange operations. Along with domestic banks, the foreign banks are also compelled to furnish the prescribed returns to the Government. In Japan, a foreign bank has to obtain a licence from the Government before opening a branch. The Government can either forbid the foreign bank from taking deposits or subject the bank to certain extra taxes. For every branch opened in Japan, a foreign bank is required to deposit 1,000,000 yen in the Government treasury. Australia totally forbids the establishment of a foreign bank's branch.[1]

[1] This is the reason why, in spite of its name, the Chartered Bank of India, Australia and China, for example, does not possess a single branch in Australia.

While foreign Governments have devised various measures to protect the interests of their indigenous banking institutions, non-indigenous banks in India, taking advantage of the absence of adequate Government protection to indigenous institutions, seek to consolidate their own position under regulations detrimental to the interests of indigenous banks.

The following rule of the Exchange Banks' Association, Bombay, speaks for itself and shows its attitude towards non-member banks, who are mostly indigenous:—

> "Brokerage on Sterling and other Exchange sales to merchants shall not be less than $\frac{1}{16}$ per cent and to all Banks $\frac{1}{32}$ per cent with the following exceptions:—
>
> Imperial Bank of India
> Bank of Baroda
> Allahabad Bank
> Central Bank of India
> Grindlay & Co.
> Thomas Cook & Son."

Thus all banks who are members of the Exchange Banks' Association can sell on London through their certified brokers by paying $\frac{1}{32}$ per cent brokerage, but there is a mandate to these brokers to charge not less than $\frac{1}{16}$ per cent brokerage to the above banks and thus render exchange business costlier for them than to the member-banks.

It is true that the Chairman of the Exchange Banks' Association has invited the Imperial Bank, the Central Bank and perhaps some other banks to join their Association and abide by their rules. There are, however, certain difficulties in the way of indigenous banks joining the Association. One of them is that the interests of the Exchange Banks are bound often to prove conflicting with those of the indigenous banks; and the latter, being in a minority, would naturally feel that their best interests might not always be adequately safeguarded. Besides, if the Exchange Banks, in existing circumstances, are allowed a free hand to finance the internal trade of the country

and enter into direct and unfettered competition with the indigenous banks, there appears no reason why the indigenous banks should be saddled with a disability of the nature referred to above in respect of their exchange business.

We appreciate that the Exchange Banks have played a useful part in the financing of India's foreign trade, but when they prove, as at present, a menace to the progress of Indian banks, the need for restrictive legislation appears imperative. The economic prosperity of India depends to a large extent on the development of indigenous banking institutions, and it is, therefore, the foremost duty of the Government and the Reserve Bank to protect their interests against the unjustifiable competition of these more powerful foreign rivals.

The public, undoubtedly, could do a lot through encouraging and supporting their own banks, and even if they resolve to deal with sound indigenous banks on equal terms with their rivals, the large amount of money now deposited with non-indigenous banks can be secured by sound indigenous institutions at a lower rate of interest than at present, enabling them thereby to compete successfully with foreign banks.

Indian Joint-Stock Banks

Bank failures and their causes.—Though the Indian Joint-Stock Banks came on the scene later than some of the Exchange Banks, they have always been taking a leading part in spreading the banking habit amongst the vast millions of the population. Their history is, however, one tale of vicissitudes, and if, in spite of all the travail and tribulations which have been their lot throughout, they are to-day flourishing in their present numbers, the major portion of the credit must go to the pioneers who have conclusively demonstrated to an incredulous public that the successful working of an Indian Joint-Stock Bank is not an idle dream but a practical proposition. It is, however, necessary to emphasise the one important fact that, ultimately, the growth of indigenous banking institutions depends to a considerable extent on the

active support which the people at large are prepared to accord to them. It has been admitted on all hands that the healthy development of banks of Indian origin is a *sine qua non* of national regeneration, and this would be impossible of achievement unless the sympathy, confidence and co-operation of the public are forthcoming in a large measure.

While it is true that, in comparison with conditions as they were years ago, the later progress of the Indian Joint-Stock Banks has been noteworthy, we should not lose sight of the fact that they are still being overshadowed by their foreign rivals and that they have not yet attained that position of pre-eminence which is their legitimate due. Among the many factors responsible for this present backwardness is the lack of faith of the Indian public in indigenous banks. The general predilection in favour of foreign institutions still persists. This is due in part to the fact that Indian depositors have suffered in the past by placing their trust in some Indian banks which did not merit such trust. While this has been the unhappy experience in certain cases, that by itself is not sufficient reason for concluding that no Indian-managed bank can be secure. The past failures of the Indian banks must be viewed in their proper perspective and proportion. There is not one country in the world which has not passed through the ordeal of crises and banking failures at one stage or the other of its banking history. Efficiency is not the sole prerogative of foreign institutions, nor is mismanagement peculiar to Indian banks alone. When the banking system of a country is in its infancy, it should not be a surprise if failures do occur. The phenomenon of bank failures is common to all countries, and India can be no exception. Even in the advanced Western countries we come across many instances of big banks closing their doors. If we compare the number of bank failures in India with that in even the progressive European countries or in the United States of America, we find that we have no need to be ashamed. It has been ascertained that during the ten years 1921–30 the bank suspensions in America numbered 6,623, while during the

same period the number of banks that failed in India was only 143. Bank failures, therefore, are by no means confined to India, and the comparatively negligible number of failures that has occurred in the past should be sufficient proof that there is no inherent inefficiency in Indian banks as such. A blind preference for foreign banks is, therefore, "tantamount to placing a handicap on the national and offering a bounty to the foreign enterprises," as Mr. N. R. Sircar has remarked in his minute of dissent to the Indian Central Banking Enquiry Committee Report.

A brief examination of the chief causes that contributed to bank failures in our country in the past would serve as a valuable guide and would enable Indian banks of the present and the future to profit by the previous bitter experiences and avoid the shoals and rocks on which many of their predecessors floundered.

The main defects of the Indian Joint-Stock Banks in the past can be classified under two categories—internal drawbacks and external handicaps.

Among the former, it has been noticed that inexperience in the modern methods of bank management was the chief defect in the earlier years. In describing the crisis of 1913–14, Mr. Findlay Shirras refers to the rapid establishment of numerous banks without experienced bankers at their head and says that "it was a case of an army going into battle without any trained officers and without any orders from the General Staff." The lack of opportunities for learning the intricacies of Western banking methods was an important reason for the inexperience of the bank officers of those days.

It is also unfortunately true that the Managers and Directors of the Indian banks of the past did not display that amount of integrity and straight-forwardness that is demanded of bankers, and they were bent more upon the speedy accumulation of riches for themselves than on safeguarding the interests of depositors and shareholders. In order to achieve this selfish end, they indulged in dishonest transactions and wild speculation. In their anxiety to gratify their get-rich-quick desire they threw discretion to

the winds and advanced large sums on securities not worth a name. They declared large dividends even in the initial stages without attempting to build up substantial reserves for the rainy day. Their most serious crime lay in their transgressing the limits of legitimate banking business by giving preference to ordinary trading business. As Sir T. Smith of the Allahabad Bank said in his evidence before the Indian Industrial Commission, some of these so-called "banks" included in their banking business such fantastic enterprises as coach-building and medical attendance. It is no wonder, therefore, that when the crash came it shattered most of the banks.

The danger arising from the establishment of banks with insufficient capital was fully discussed by the Central Banking Enquiry Committee. They have referred at length to the risks involved in such a situation and have pointed out glaring instances of banks with ridiculously low paid-up capital. For example, they have observed that out of the 16 banks that failed in 1927, 6 had practically no paid-up capital, one had a paid-up capital of Rs. 800 and another of Rs. 1,400! Small banks have taken advantage of the absence of any provision in the Indian Companies' Act stipulating a minimum paid-up capital.

This evil feature, namely, the springing up of mushroom banks without sufficient capital, is still prevalent in some parts of the country. In Travancore, for instance, many so-called banks have been started with a low capital of Rs. 1,000. But this tendency is most marked in Bengal where, in addition to as many as 782 Loan Offices, there are a large number of banks without paid-up capital of even Rs. 1 lakh. What is even more alarming is the great disparity between their deposits and their capital. In one instance the paid-up capital together with the reserve was only 3·45 lakhs, while the deposits were 63·10 lakhs. If in this case, a depreciation of even 10 per cent were to occur in the investments which came to 33·68 lakhs apart from the question of bad debts in time of trade depression practically the whole of the capital and reserve would vanish giving no security of bank's capital to depositors.

Again, the cash position of the small banks is not always quite satisfactory, nor is the liquidity of their investments beyond doubt. The depositors, therefore, cannot long enjoy a sense of security. Further, it is apparent that in order to attract such a large volume of deposits, the small banks should necessarily offer handsome rates of interest, and naturally, in their turn, they will also have to make their advances at high rates without adequate securities. It should be remembered in this connection that while nowadays it is very easy for any sound business to obtain the requisite funds at reasonably low rates, it is only the promoters of risky and hazardous enterprises that would think of going in for advances from these small banks at high rates of interest. Thus, in effect, it amounts to this, that the small banks lend even to third-rate business concerns, and the attendant risks are consequently greater. If some such business fails, as it well might, the loss to the bank would be great, and so it would try to keep it a secret without disclosing it in the balance sheet.

The scanty capital of these banks and the wide divergence between capital and deposits and the inexperienced men at the helm of such institutions are constant sources of danger to Indian banking in general; for, should a big loss occur at any time, most of the banks with such abnormally low capital would find themselves in a precarious position and the result would be that the public would lose confidence in indigenous institutions and would become panicky. Another serious set-back in the progress of Indian banking would naturally follow.

If such a calamity is to be averted, remedial measures should be thought of immediately. The ever-increasing growth in the number of small banks has to be checked, and their place should be taken by a smaller number of banks with greater capital resources and reserves. This should be brought about, if necessary, by the amalgamation of a number of small banking institutions. In the larger interests of the development of Indian banking along right channels, the question of inserting specific provisions in the Companies' Act regarding the minimum capital of

banks and percentage of paid-up capital to deposits should also be investigated by the Government. The absence of any comprehensive bank law, as we find in the Canadian Bank Act, has made the incorporation of numerous small and unstable banks far too easy. It is, therefore, necessary that suitable legislative measures are enacted at an early date to overcome this danger.

The public distrust of Indian management to which reference has been made, though not as great or as universal to-day as it was some years ago, does yet linger. The cause and the effect are thus intertwined and the vicious circle is there to make Indian banks still lag behind.

We also find that, apart from the formidable competition of the Imperial Bank and the non-indigenous banks, among the Indian banks themselves there prevail mutual jealousy and envy, and they seldom unite even in the face of the difficulties that confront them to-day.

Yet, in spite of their woes, the Indian Joint-Stock Banks have managed to survive largely by dint of their stamina. Indeed, it is astonishing that they are functioning to-day in such large numbers. Their past achievements lend strength to the belief that, given a larger measure of Government support and with a more active manifestation of public solicitude, it should not at all be difficult for them to achieve still greater triumphs in the future. The soil for their growth continues to be fertile, though the presence of thorny shrubs has considerably detracted from the fertility. All that is needed, therefore, is a thorough and systematic process of weeding out, and when that is effected the risks of failures would be greatly minimised even if they be not completely eliminated, and the hardy plant of Indian joint-stock banking will thrive quicker and better.

Indigenous Bankers

Their importance, merits and demerits.—From time immemorial the indigenous bankers have been rendering valuable service in the financing of the internal trade. They are distributed throughout the length and breadth of the country and

go by different names, such as Shroffs, Mahajans, Sowcars, Chettiars, Banias, Nanavaties, etc. The Shroff is the connecting link between the banks on the one hand and the vast trading community on the other. He buys the *hundis* either from the traders directly or from other smaller Shroffs, at a high rate of discount. It is only when he has not sufficient money of his own to carry on this business that he seeks the aid of the banks by rediscounting with them the *hundis* which he holds.

The indigenous banker occupies an important place in the rural society and acts not only as the moneylender but also as the village shopkeeper and as the purchaser of rural produce either on his own account or on behalf of big exporting firms. This concentration of diverse functions in a single individual places the borrowing agriculturist at a decided disadvantage. As Sir Daniel Hamilton observed, whereas "the secret of successful industry is to buy your finance cheap and to sell your produce dear, the Indian buys his finance dear and sells his produce cheap, as his creditor generally fixes the price of both." By concentrating all the power in his own hands, the rural indigenous banker has been able to exact unconscionably high rates of interest and also to impose iniquitous restrictions on the borrowers.

At the same time, the indigenous banker is not, after all, the cruel Shylock that he is sometimes represented to be. "He has met the needs of the agriculturist with a curious blend of severity and sympathy" and has shown himself ready to postpone recovery if and when the borrower was in straitened circumstances and expressed inability to repay his loan on the due date. As Sir Osborne Smith has remarked, "it is questionable whether a banking system which provided a much lower rate of interest but expected punctual repayments or sale of land would have been more welcome to the cultivators." With all his defects—and they are admittedly numerous—the indigenous banker has a definite place in the banking organisation. The fault lies not so much with the Mahajan as with the indigenous banking system itself which has not been organised on scientific lines; and the remedy should, therefore, be sought in

remoulding the system to suit present-day conditions rather than in trying to do away completely with the much-maligned Mahajan.

If the native bankers had concentrated on banking business alone they might have retained their greatness, but, instead, they combined trading with banking with disastrous results in most cases. Again, their calling was usually hereditary, and the prosperity, therefore, of a firm of indigenous bankers depended almost entirely upon the capacity of the person at its helm. The inefficiency of successors was the principal cause of failures among indigenous banking firms, but, more than everything else, the ever-increasing competition which the indigenous banker began to experience from the Imperial Bank and the Indian Joint-Stock Banks led to his being gradually ousted from the field of remittance business and other profitable branches of work. These banks gradually opened branches even in small towns where previously the Shroff had exercised unrestricted sway, and it was not difficult for them with their greater resources and better organisation to quote more favourable terms and capture the greater portion of their business. But the modern commercial banks have not yet penetrated into the interior and, therefore, the rural population has only one source to resort to when it is in need of money, and that is the indigenous banker. But for him they would have to go without any financial assistance whatever. If the question was viewed in this light, it would be realised how indispensable he is, particularly in the rural economy of the country.

Professor C. N. Vakil has pointed out in a recent issue of the *Times of India* how even to-day out of the large volume of internal trade valued approximately at Rs. 5,000 crores, only a small fraction, representing about Rs. 100 crores, is being financed by all the Scheduled Banks together. The financing of by far the largest portion of the internal trade still remains in the hands of the indigenous bankers. The greatest need, therefore, at the present moment is to cleanse and purify the indigenous system and then to fit it in an appropriate place within the framework. The Central

Banking Enquiry Committee devoted a considerable portion of their time to the examination of this problem, and, being impressed by the unanimity of opinion expressed on all sides, recommended that such of the indigenous bankers who may be prepared to drop all non-banking activities and also to abide by certain conditions and regulations regarding the proper maintenance of accounts and such other details, should be included in the list of "Scheduled Banks." Though the Reserve Bank Act, as it stands now, does not specifically include them in the schedule as recommended, it contains a clause requiring the bank to study the whole question of indigenous bankers and to submit to Government within three years concrete proposals for bringing them within the banking structure and extending to them all the privileges and responsibilities of Scheduled Banks.

Sir George Schuster stressed the need for determining the future rôle of the indigenous bankers when, in introducing the Reserve Bank Bill, he declared in the Legislative Assembly as follows:—

"It is impossible to overestimate the importance of the part that the indigenous banker plays in the whole of the banking and credit machinery in India. I want to make it quite clear that we recognise that until the vast portion of India's banking and credit machinery that is represented by the indigenous bankers is put into gear with the relatively small machine of the modernised money market with the Reserve Bank as its central control, it will be impossible for the Reserve Bank to exercise full control over the currency and credit of India." Great as has been the indigenous banker's contribution in the past in meeting the banking needs of the country, a still greater future awaits him. But it is necessary that, in order to achieve this, he should, in the first place, shed his non-banking activities and medieval methods. He should also move with the times and adapt himself to the change of environments. If he does this, he could greatly enhance his usefulness to society.

Co-operative Banks

Owing to the limitations of space and the lack of intimate or direct contact on the writer's part with the Co-operative movement, no more than a passing reference to it can be attempted at this stage. It has to be observed that there is no unanimity of opinion as to the extent of its benefit to the community. But, nevertheless, it cannot be denied that Co-operative Banks do form part and parcel of the country's banking structure, and that they have achieved a certain measure of success in their own way. Under the Reserve Bank Act, all the rights and privileges of the Scheduled Banks are extended to them also, and with such advantages their usefulness to the rural population may be expected to increase in the future.

General

Great scope for development.—The following table, showing the paid-up capital and reserves and the deposits of the three important classes of banks in India, compares the pre-war position with that of recent years :—

Paid-up Capital, Reserves and Deposits as at December 31 of each Year

(Statistical Tables relating to Banks in India)

Year	*Imperial Bank of India (prior to Jan. 27, 1921, Presidency Banks)*			*Exchange Banks*			*Indian Joint-Stock Banks*			*Total*		
	No.	*Capital and Reserves (thousands of Rs.)*	*Deposits (thousands of Rs.)*	*No.*	*Capital and Reserves (thousands of Rs.)*	*Deposits in India (thousands of Rs.)*	*No.*	*Capital and Reserves (thousands of Rs.)*	*Deposits (thousands of Rs.)*	*No.*	*Capital and Reserves (thousands of Rs.)*	*Deposits (thousands of Rs.)*
1913	3	7,48,07	42,37,16	12	50,43,33	31,03,46	41	4,14,00	24,10,00	56	62,05,40	97,50,62
(Pre-War) Presidency Banks.												
1920	3	7,52,79	87,04,53	15	1,20,28,93	74,80,71	58	11,73,85	73,48,10	76	1,39,55,57	2,35,33,34
1926	1	10,72,00	80,35,06	18	1,97,33,73	71,54,22	75	12,10,33	63,14,99	94	2,20,16,11	2,15,04,27
1932	1	11,05,46	75,43,30	18	2,31,79,47	73,06,56	83	13,41,72	76,16,04	102	2,56,26,65	2,24,65,90
1934	1	11,28,00	81,02,00	17	1,88,83,00	71,40,00	105	14,16,00	81,88,00	123	2,14,27,00	2,34,30,00

While the figures quoted above indicate progress, it should be recognised that there is much leeway to be made up if India desires to take her place among the advanced nations of the world. Indeed, India's backwardness in the development of banking has become almost notorious and has been emphasised more than once by individual writers and official bodies alike. The Indian Industrial Commission and the External Capital Committee, for instance, drew pointed attention to the fact that India, with a sixth of the world's total population, is most inadequately provided with banking facilities. There are no banks in the 700,000 villages of India, nor is the position much better even in the towns, for only 480 out of 2,500 of the latter can boast of banking offices. This paucity of banking facilities is further illustrated by the following statement comparing this country with some of the advanced Western countries:—

Country	*Population in Millions*	*Number of Bank Offices*	*No. of Bank Offices per million persons*
Canada . .	10	3,772	377
United Kingdom .	46	10,066	219
U.S.A. . .	119	18,067	152
India . . .	353	1,269	3·6

Statistical analysis has also revealed that the total volume of deposits attracted by all the banks in India cannot stand comparison with the deposit figures of even one of the "Big Five" in England.

Deposits as on December 31, 1924

Imperial Bank of India, Exchange Banks and the Indian Joint-Stock Banks	£158 millions (Rs. 210 crores at 1*s.* 6*d.* per rupee).
Midland Bank Ltd.	£382 millions
Lloyds Bank Ltd.	£366 ,,
Barclays Bank Ltd.	£325 ,,
Westminster Bank Ltd. . . .	£292 ,,
National Provincial Bank Ltd. . .	£275 ,,

It has also been computed that the average deposit per head in India works out only at 15*s.* as compared with £73 and £57 in the United States of America and Great

Britain respectively. The total value of the cheques handled by the clearing houses in various countries is another index of the prevalence of the banking habit among the people. Even in this comparison India pales into insignificance; for, while the aggregate value of the cheques cleared through the London clearing house alone during the year 1931 amounted to £36,236 millions, the corresponding total figure for all the seven clearing houses in India for the same year was only £1,171 millions (Rs. 15,61,50 lakhs @ sh. 1*s.* 6*d.*).

All these go to show that the banking habit has not taken root and has not permeated among all sections of the population. Only the urban areas have been served by banks, the vast and scattered rural population still remaining untouched. The scope, therefore, for the extension of the benefit of modern banking methods is very vast. With the encouragement and active assistance of the Reserve Bank, the Indian Joint-Stock Banks could extend their spheres of usefulness and help in the mobilisation of the country's financial resources by releasing the money that lies dormant in endless small hoards in the villages of India.

Banking in its essentials has been known in India for ages, but, although India evolved and worked the principles of banking prior to the Western countries, the West definitely is now well ahead of the East in the matter of system. India, in particular, is extremely backward in modern organised banking, and this fact is driven home to us when we compare the savings of £50 per head in the United Kingdom with those of 7*s.* 8*d.* in India. The gap, wide as it is, must be gradually filled in and this could only be done through a rapid development of Indian banking on the right lines.

The prosperity of a country depends upon its economic activities. It is agriculture, commerce and industry that provide a country's wealth, but without adequate banking facilities these three cannot flourish. For a vigorous economic life a fully-developed banking system is highly essential, and strong nationalised banking alone can provide the necessary leverage for the economic uplift of the country.

Postscript, July, 31, 1938.—Since the above lines were written by the late Sir S. N. Pochkhanwala, the founder of the greatest Indian Joint-Stock Bank with Indian capital and Indian management, legislative regulation of the smaller joint-stock banks has been provided for under the Indian Companies Amendment Act, 1936, Part XA, Sections 277F to 277N. Among other things, it defines a bank, and lays down that a bank must not be managed by a managing agent, must not start business unless it has received paid-up capital of at least Rs. 50,000, must allot at least 20 per cent of the annual profits to the Reserve Fund till the Reserve Fund is equal to the paid-up capital, must maintain a cash-reserve equal to 1½ per cent of time liabilities and 5 per cent of demand liabilities, and must supply to the Registrar of Joint-Stock Companies monthly statements regarding cash reserves and liabilities as on each Friday of the previous month. These provisions of the new law are likely to strengthen the banking structure by promoting amalgamation of tiny banks and by bringing the smaller joint-stock banks into closer relations with the scheduled banks. The Reserve Bank has also recently drawn up a scheme designed to establish links between the indigenous bankers and moneylenders on the one hand and the joint-stock banks and the Reserve Bank on the other. —*Editors.*

CHAPTER XXX

THE RESERVE BANK OF INDIA

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I

§ 1. The efforts involved in the passage through the Legislatures of the Reserve Bank of India Act, which received the assent of the Governor-General on March 6, 1934, did not represent the first serious attempt to establish a Reserve Bank in India. Besides the Reserve Bank Bill which was thrown out by the Legislative Assembly in 1928, there were several schemes proposed from time to time which were similarly set aside, although by different authorities. Treatises on Indian Banking, in their passing references to the subject, state that the first proposal of the kind was made in 1836.[1] But there were two interesting schemes before that date.[2] Warren Hastings was responsible for the one in 1773,[3] and Robert Rickards, a member of the Government of Bombay, for the second in 1808.[4]

Early central banking proposals.—The first of these was more than a mere proposal, as the bank was working for some time before it was dissolved by order of the Company's Directors in England. It was the result of a "Plan for a General Bank in Bengal and Bahar [sic]"[5], placed before the Board of Revenue in January, 1773, by Warren Hastings. It is interesting

[1] *e.g.*, J. M. Keynes, *Indian Currency and Finance*, p. 233.

[2] For a somewhat detailed review of the schemes see an article by me on "Some Aspects of a Central Reserve Bank for India—I," *Asiatic Review*, Vol. 29, October, 1933, p. 491 *et seq.*

[3] *India Office Records, Miscellaneous Despatches*, Vol. 776, p. 209 *et seq.*

[4] *Parliamentary Papers*, 1812–13, Vol. X, p. 261 *et seq.*

[5] If we ignore the Northern Circars and the possessions round Madras, Bengal and *Bahar* comprised British territory in India at that date.

to note that the Bank was intended to act, as bankers to the Government, with a view to remedying the inconveniences caused by the withdrawal of funds into the Company's treasury in times of revenue collections; to work as an agency for providing easy and cheap means of remittance of funds round the country; and to enforce the currency of "Sicca" rupees as the standard coin of the country. "For want of time and ability in the Government either to superintend or control so complicated a business" it was decided that the Bank was not to be on the Company's "own immediate account" but only a private concern. Accordingly two celebrated merchant bankers of the time[1] in India were appointed jointly to constitute the Bank. Considering that in the early seventies of the eighteenth century banking in the modern sense of the term was still in its period of inception, and central banking theory, as such, was yet to be formulated, the "General Bank" of 1773, was perhaps not a poor beginning. It is interesting to note that the Bank of England did not at this time possess the privilege of the custody of Public Revenues[2] which Hastings' bank did.

§ 2. Rickards' scheme was more elaborately planned and perhaps is superior to the first in many respects. It was formulated in a memorandum presented by him to the Government of Bengal (which was then the "central" Government) in 1808, *i.e.*, about two years after the establishment of the Bank of Bengal. The Bank was not to be a State Bank, nor was it to be a purely private institution. Rickards was alive to the dangers of both. It was, therefore, to be a quasi-public institution with a Board of Directors consisting of one Government nominee and half a dozen or so "independent men." It was to have three head offices, one each at Bombay, Calcutta and Madras, with "subordinate Banks or offices" round the country. In

[1] They were "Bauboo Hazzurimull and Roy Dalchand, the former an ancient and respectable merchant of Calcutta, the latter a banker at Moorshidabad, and a branch of the family of Jaggatseat." *India Office Records*, op. cit., p. 229.

[2] Philippovich, *History of the Bank of England* (Nat. Mon. Com.), pp. 143 and 183 *et seq.* Also, Andreades, *History of Bank of England*, p. 393 *et seq.*

this he anticipated the constitution of the Imperial Bank of India. The Bank was to have the right, and presumably the monopoly of note issue; it was to act as bankers to the Government; be the centre and head of the money market; control and co-ordinate its constituents; provide for the free flow of funds round the country; bring about a smoothening out of the divergences in the money rates as between seasons, and different parts of the country; and perhaps also control the exchange rate. The project, however, was not sympathetically viewed by the Governor-General and was rejected by the Court of Directors.

§ 3. The next proposal for the establishment of a central bank was made in 1836, by a body of "East India Merchants." Besides transacting some of the central banking functions, it was also expected, by the authors, to be instrumental in providing employment for the "redundant capital" of Great Britain. But the Bank of Bengal having agreed to take over all the duties expected of the new bank, the project fell through. After this date, incidental allusions in official correspondence to the establishment of a central bank are numerous. And after the establishment of the Banks of Bombay (1840) and Madras (1843), these allusions were sometimes in the direction of amalgamating the three Presidency Banks. In this connection mention may be made of Wilson's scheme (1859) for a Government Issue Department, and Dickson's memorandum, on failure of the Bank of Bombay (1868), for the amalgamation of the three Presidency Banks. In 1898, some of the witnesses before the Fowler Committee supported the idea of a central bank and, Alfred Rothschild, in a written statement outlined a plan for one, on the model of the Bank of England. The Committee, however, regarded the question as outside their terms of reference and did not pay attention to it in their report. But Humbro, one of the members, in a separate note pointed out the importance of a central bank. This note, after some correspondence, gave rise to a conference of the representatives of Provincial Governments, Presidency Banks, and Chambers of Commerce. Before the conference,

Dawkins, the Finance Member, placed a scheme for an Indian Central Bank. The Secretary of State, however, set it aside. Thereafter, Sir Edward Law examined the question of amalgamating the Presidency Banks, but abandoned the idea on the ground that the cost would be too high. The appointment of the Chamberlain Commission (1913) again brought the question to prominence: two memoranda were placed before the Commission, one by Sir Lionel Abrahams, and the other by Mr. Keynes. The terms of reference of the Babington Smith Committee did not include examination of the question of a central bank.

§ 4. **Sir Basil Blackett's Bill.**—The amalgamation of the Presidency Banks in 1921, into the Imperial Bank of India, did not put an end either to the demand or to the necessity, for a central bank. The question, therefore, was again raised by and before the Hilton Young Commission, 1926. The Commission recommended the establishment of a Central Reserve Bank and outlined a constitution for one. Based on this, the late Sir Basil Blackett, the Finance Member, introduced a Bill in the Legislative Assembly on January 25, 1927. From the very start the Assembly showed a lack of enthusiasm for the measure, and when the Bill emerged from the hands of the Joint Select Committee, in all essentials it was very much different from the original. The private bank was turned into a State bank, and, the Legislatures and special interests like the Chambers of Commerce, specifically disqualified for seats on the Directorate of the Bank, in the original Bill, were allowed such representation. After the first seven clauses of the Bill, as reported by the Committee, were considered and voted upon, further consideration of it was postponed, on the request of the Finance Member, to allow him time to come to an understanding with the Legislature on the question of composition of the Board. Since no satisfactory agreement could be arrived at on the point, the Government decided not to proceed further with the Bill.

Thereafter, Sir Basil Blackett paid a visit to England,

and, on return, had published in the *Gazette of India*, on January 14, 1928, another Reserve Bank of India Bill, providing for a shareholders' Bank, "free from political influence." But, President Patel refused to call the Government to introduce the new Bill, which was put on the agenda of the House for February 1, 1928, on the ground, that no new Bill could be introduced on a topic, when a Bill was already before the House on it, unless the first one was withdrawn. This could be done, however, he maintained, only if the House allowed leave to do so. The Finance Member thereupon decided to proceed with the old Bill, but could not go beyond clause 8, which was rejected by a majority of one. The clause related to the Board of Management, and since no Reserve Bank could function without one, further deliberations on the Bill were dropped. Thus terminated the heroic efforts of Sir Basil Blackett to see himself father to an Indian Reserve Bank.

II

§ 5. The matter was again taken up by the Government of India in their Despatch, dated September 20, 1930, on the Simon Commission's Reform Proposals, which stated that, "the formation of a reserve bank on sound lines must . . . be a condition precedent to any transfer of financial responsibility from the agent of Parliament to a minister answerable to the Indian Legislature."[1] The Government, on principle, abhorred the idea of a responsible minister having control over the currency and exchange policy of the country. These observations may be said to represent the genesis of the efforts that led to the 1934 Act. The Majority Report of the Central Banking Inquiry Committee, the Minority Report, and the Report of the Foreign Experts (1931) associated with the Committee, all emphasised the vital importance of a Reserve Bank to the country. The discussions at the three Round-Table Conferences on the subject resulted in the acceptance of the

[1] *Despatch*, p. 150.

view expressed in the Government of India Despatch. The "White Paper" on the proposals for Indian Constitutional Reform, published in March, 1933, laid down among the financial prerequisites to the inauguration of a responsible Federal Government that a Reserve Bank, "free from political influence, will have been set up by Indian Legislation and be already successfully operating" (para. 32).

The Reserve Bank of India Act, 1934.—And, in accordance with the undertaking given by him to the Third Round-Table Conference, the Secretary of State set up a Committee on Indian Reserve Bank Legislation, which met in London in July, 1933. On the basis of the Report of this Committee a Bill was introduced in the Legislative Assembly in September, 1933. Unlike in 1927, the Congress Party being now out of the Assembly, the Bill of 1933, without material alterations, passed through both Houses of Legislature by February, 1934, and the Act, as already noted, received the assent of the Governor-General on March 6, of the same year. Thus, it was left to Sir George Schuster to realise the ambition of his predecessor. Preparations were then made for the inauguration of the Bank.

The capital was issued to the public between March 22 and March 25, 1935, and was heavily over-subscribed, the applications being for Rs. 9 crores' worth of shares. Considering the low rate of dividend offered (3½ per cent), this is due in the main, no doubt, to the redundant funds in the market which, owing to the depression, find the scope for safe and attractive investment limited or almost absent.

§ 6. **Constitution of the bank.**—The Act is divided into four chapters and five schedules. The chapters deal with definitions; incorporation, share capital, management, and business of the Bank; central banking functions; and with general provisions relating to the Reserve Fund, Agricultural Credit Department, auditing, returns, and kindred questions. The schedules comprise the areas served by the various Share Registers; provisions to be embodied in the agreement

between the Reserve Bank and the Imperial Bank of India; scale of additional dividend payable to shareholders; and a form giving details of the weekly return to be published.

The share capital of the Bank is 5 crores of rupees divided into shares of one hundred rupees each publicly subscribed and fully paid up. There are five separate Registers of shareholders maintained severally at Bombay, Calcutta, Delhi, Madras, and Rangoon, and the shares assigned to each Register are fixed. In this, weightage has been given to Delhi, at the expense of Madras and Rangoon. Ownership of shares is not restricted to Indians; it is open to all citizens of the Empire. But the privilege is withheld from non-British subjects.

§ 7. The constitution of the Bank has the semblance of a federal one. It provides for a Central Board of Directors with five Local Boards, one each at Bombay, Delhi, Calcutta, Rangoon, and Madras. But the Local Boards, unless a convention giving it more powers comes to be established, which, however, would seem to be extremely unlikely, would prove to be merely advisory bodies and electoral colleges to send representatives to the Central Board. Otherwise they have no specific powers, duties, or responsibilities, conferred on them by the Act. But the Central Board may, if it chooses, delegate to them whatever functions it may think fit. It would seem, therefore, that at best, they may play the part of Discount Committees of the Banks of France, Japan or Belgium.

The Central Board consists of a Governor and two Deputy Governors, appointed by the Governor-General-in-Council, after consideration of the recommendation made by the Board in that behalf; four Directors, nominated by the Governor-General-in-Council; eight Directors, elected by the elected members of the Local Boards—two from Bombay, two from Calcutta, two from Delhi, one from Madras, and one from Rangoon; and one Government official, nominated by the Governor-General-in-Council. The last-named Director and the Deputy Governors may only attend meetings of the Central Board and take part in its deliberations, but shall not be entitled to vote. The

nominated official shall hold office during the pleasure of the Governor-General, and the other Directors for five years, but shall be eligible for re-election or re-nomination, as the case may be.

Each Local Board consists of five members elected by shareholders who are registered on the register concerned, and not more than three members nominated by the Central Board from the local shareholders.

§ 8. **Functions of the bank.**—The Act lays down in detail the type of business the Bank may and may not transact. In this, experience and laws of other countries have been freely drawn upon. The Bank is designed to serve as a Bankers' Bank. In all normal times it would offer no competition to the commercial banks in the country, and if under special circumstances it should appear to do so, it would not be for making profits but merely to enforce a policy conceived to be in the best interests of the country. The Bank thus cannot own fixed property, except its own premises, nor make advances against them; offer interest on deposits, nor advance unsecured loans. Other types of business forbidden to the Bank are buying its own shares—for that would amount to reducing the capital of the Bank—buying shares of any company or bank, advancing money against them, or engaging in trade, or otherwise having a direct interest in any commercial, industrial, or other business undertaking.

§ 9. The Bank may accept deposits without interest, purchase, sell or re-discount, bills of exchange arising out of bona fide commercial or trade transactions, or issued or drawn for the purpose of holding or trading in securities of the Government of India, or a Local Government, or securities of an approved Indian State, bearing, in each case, at least two good signatures, one of which shall be that of a member bank with a maturity of ninety days (or nine months in the case of bills drawn or issued for the purpose of financing seasonal agricultural operations or the marketing of crops). The extended period in respect of agricultural bills has precedents in the U.S.A., South Africa,

Hungary, and Chile. The Bank may deal in foreign exchanges in minimum amounts of one lakh of rupees, but only with the scheduled banks, and purchase, sell or re-discount, sterling bills maturing within ninety days, also only with the scheduled banks. It may purchase or sell securities of the Government of India, the British Government, a Local Government, or an approved Indian State. It may make advances to the Provincial and Central Governments in India. No limit, however, has been put on the amount that can be so lent. Expert opinion to-day is in favour of putting such a limit, since that would remove, perhaps, the chief motive that induces most Governments, when in difficulties, to attempt to influence the management of their banks of issue. The Bank would act as banker to the Provincial and the Central Governments. It would have the monopoly of issue. For some time, however, the Bank would only issue the notes supplied to it by the Government of India, but the provisions in the Act, applicable to Bank Notes, shall apply to the Government of India notes, issued by the Bank, during the period of transition.

§ 10. **Relation with member banks.**—Following the American practice which has been generally adopted by the post-war Central Banks, it has been laid down that the member banks shall maintain with the Reserve Bank a reserve of 5 per cent. and 2 per cent. of their respective current and time liabilities. Although much can be said in favour of making a distinction between the two types of liabilities, American experience has revealed that under the circumstances banks effect a shifting of current to the time deposits, thus causing an artificial ratio between the two. A composite reserve backing might, therefore, have been preferable and it could then have been made obligatory on the banks to publish separately the figures for the two types of deposits. While satisfying the requirements of certain scientific analysis this would have removed the otherwise living temptation to tamper with facts and exhibit an unreal position.

In return for the interest-free reserve balances maintained with the Central Bank, the member banks would, for the first time in India, find in the Bank a source of emergency currency. In the past, banks, when in difficulties have suffered unnecessarily severe hardships or have been forced into liquidation, despite their sound assets, owing to the absence of assured re-discount facilities. The Reserve Bank, through its willingness to discount at all times, bills of a certain quality, at the official bank rate, published weekly, would prove of immense benefit to the banking system. It would lead to stability and inspire confidence. In view of the comparatively little opposition offered by the commercial banks in India, unlike those in America and South Africa, for instance, to the reserve backing requirements, they would seem to have a greater sense of appreciation of the advantages they would derive from the Bank. The member banks would also enjoy the benefits of clearance and collection.

Although in all normal times the Bank would offer no competition to the commercial banks, it has been empowered to carry on "open market operations," which are an essential reserve bank weapon for credit control. With the approval of the Central Board, the Bank may thus enter directly into the market, and deal in securities or eligible bills, without the signature of a scheduled bank or make loans or advances, if such action be found necessary for enforcing a certain credit policy on the market, with a view to either controlling the state of the exchanges, protecting the reserves of the country, or maintaining price stability.

§ 11. As in the case of the Commonwealth Bank of Australia, based on the model of the Bank of England, the Issue and the Banking Departments of the Reserve Bank have been separated. A British Committee of Experts (the Macmillan Committee), after subjecting this system to a severe critical analysis, had opined against the continuance of it in England, on scientific grounds, and the framers of the Act in India would seem to have paid scant courtesy to this expert opinion. The separation of the departments deprives the "reserve proportion" of the banking depart-

ment of its significance and, under it, the liabilities of the Bank are not brought out as one comprehensive whole. This practice has not featured in any of the other Central Banks.

III

§ 12. Having reviewed some of the more important provisions of the Act, we may now briefly dwell upon some of its general features, such as, the independence of the Bank from political influence, the character of the currency standard and the currency system, and the Agricultural Credit Department.

Independence of the Bank.—Certain critics of the Act have maintained that a cardinal feature of the Reserve Bank is its freedom from political influence. The Government in India as well as the Secretary of State seem to be fully satisfied about it. The importance attached to this independence was so great that, as noted above, it was officially laid down that on this, among one or two other factors, would depend the introduction of financial responsibility at the Centre in the new constitution. It may be worth while, therefore, enquiring into the character of the Bank's independence.

As evidence of this it is pointed out that the majority of the Directors (eight) are elected by the shareholders—some seem to ignore that this election is indirect—and that only a minority (six voting Directors) are nominees of the Governor-General. On closer examination, however, it would appear that this majority is an extremely precarious one, and the independence, almost wholly illusory.

§ 13. It is commonly observed that, by virtue of his position as head of the Board, and being a whole-time servant of the Bank, the Governor of a Reserve Bank wields enormous powers in practice, whatever may be the provisions of the constitution. In India, he would be a nominee of the Governor-General, would hold office for a period of five years, and would be eligible for re-appointment.

The Governor-General may remove him from office at will. Under the circumstances, the mettle of his make-up should be superhuman, if he is not to prove a mere instrument in the hands of his master. But if there exist identity of interests—this can be secured by selecting the right person—between the Governor and the Governor-General, there may never arise an occasion for the former to feel that he can only hold office during the pleasure of the latter. In no case, however, could he act with impunity in a manner prejudicial to the interests of the forces that guide the actions of the Governor-General.

§ 14. **Position of the Board of Directors.**—The position of the Board of Directors is not far different. Like the Governor of the Bank, it would also be under the influence of the Governor-General. The nominated group in the Board, including the head of the Bank, would comprise six voters in a body of fourteen voting members. But for the Board to give approval to any of his measures it would suffice if the Governor-General could get the support of one among the eight elected Directors. Circumstanced as we are to-day, it is an extreme theoretical possibility, not worth much practical notice, that all these eight would uniformly resist the wooing of the head of the State, either directly or through his agents. Perhaps wooing would be unnecessary, for, in all probability, among the elected Directors there would be one or two, if not more, who would represent the forces that be or owe their position to them. With one to vote with the nominated group, there results a tie which simplifies matters. Under it the Governor of the Bank has an additional casting vote.

The election to the Central Board is indirect and constituencies of five voters would elect one or two Directors. In the circumstances suffice it to observe that the machinery of indirect election is known to be a fertile bed for corruption of all kinds.

§ 15. The Act lays down that with a majority of nine, the Board may recommend to the Governor-General, the removal from office of any Director. This provision seems

to have no precedent and has vicious possibilities. With the elected group to vote with him, if he can find two more to concur, the Governor, under it, is in a position to intimidate any Director into submission with the threat of expulsion.

§ 16. It is not obligatory on the Governor to convene meetings of the Board oftener than six times a year, if at least one falls in a quarter, unless requisitioned by three Directors. This contrasts with the weekly meetings in the case of the Bank of England. The opportunities for the Board to influence the Governor are thus few and far between. This enhances the importance of his position and ordinarily the Board would prove to be only a body for "post mortem" deliberation meeting merely to endorse and compliment the doings of its chief.

§ 17. As if this were not enough to keep off "political influence" from the Bank, it is provided in the Act that the first Board shall wholly comprise nominated Directors. The elected element would come in only by instalments at intervals of twelve months, the first batch being elected a year after the nomination of the first Board. It is only at the close of five years that the full strength of the elected Directors would be on the Board. Till then no wooing would be necessary to secure a majority on the Board, and unless the last register to send its representatives happens to be either Rangoon or Madras, the Governor would have the requisite majority of votes for threatening with expulsion any new-comer. Thus each batch of elected Directors will soon come to learn good behaviour. This reminds one of how tamed elephants are made use of to domesticate the newly-captured wild ones!

§ 18. At the close of the period of five years it would be time for the first elected representatives to retire or seek re-election. It would be in their interest, therefore, not to displease the Governor or the Government. For, by doing so, they would be earning their opposition, while by not doing so, perhaps, earning their support in the election. Each year there would thus be retiring Directors who would not easily flout the wishes of the Governor unless

they be certain of their seats or do not intend seeking re-election.

But perhaps many of these latent "safeguards" may not have to be invoked. For, very probably, the first nominees of the Governor-General will find it possible to get themselves elected and re-elected, until they voluntarily retire, somewhat in the manner of the Directors of the Imperial Bank of India.

§ 19. **Shareholders' control.**—Little need now be said about the shareholders' control of their Reserve Bank. The general meeting of the shareholders has little power over the Bank's executive. The shares being scattered round the country, in units of five, the attendance of shareholders in person would be meagre. The primary motive for exercising any influence on their part is absent, for the schedule of dividend is fixed and would be forthcoming in due regularity, not owing to any desire on the part of the management to placate their masters, but because the credit of the institution would demand it. The only control the shareholders would have over the management is indirect *via* the Local Boards which, by turns, once in five years, would elect Directors to the Central Board; and, in view of the weak position of the latter, this control is of little practical value.

§ 20. The Reserve Bank is the nerve centre of a country's financial system. National control over its management is of vital importance, and the whole controversy over the character of this management, resolves itself into the question of what is the best means of ensuring that it would serve only national, and not purely sectional, ends. The objection against State ownership or State management of one school, or against private ownership or private management of the other, is based, that is to say, on this consideration solely. If from the situation concerned it is patent that one type of management would serve the end better than the other, all controversy on the subject ceases, or should cease. State management or private management are not ends in themselves. They are only means to an end, and there exist Reserve Banks of both the

types functioning successfully. It is thus the particular environment that largely decides what the character of the management should be.

Past experience has shown that, generally speaking, on most vital economic issues, there does not exist in India identity of views, between the rulers and the ruled. The constitution of the Reserve Bank ensures that it shall, under no circumstances, act contrary to the wishes of the Governor-General. It does not ensure that the Bank shall always be guided, whatever the Imperial requirements may be, by the larger interests of the country solely. On the contrary, there exist a series of barriers which would prevent the Bank from being influenced by such interests, as expert Indian opinion may conceive them. While the doors are kept open for the entry of one set of influences, they are closed, barred, and bolted against the other.

§ 21. **The currency system.**—We may now consider the changes effected by the Act in the character of the currency system and the currency standard. Before the Reserve Bank Act came into force the Indian currency system consisted of rupee notes, the issue of which was regulated by law, based on the British model, and rupee coins with no statutory limit as to their issue, although like the former the latter, too, were notes but "printed on silver," and in the issue of which, as in the first case, the State had absolute monopoly, the mints being closed to the public. The position was thus anomalous in the extreme: unlike in other countries, in India, only one part of the fiduciary issue was subject to statutory regulation, while the other was left to the arbitrary discretion of the currency authority. As a consequence, the total volume of currency in circulation depended on what the State wanted, or made it to be. But this freedom was tempered by the necessity of having to maintain the exchange rate of the rupee which was fixed in terms of sterling.

This situation differs from that of other countries even on exchange standards, inasmuch as, in their case, not only the gold content, or the exchange value, as the case

may be, of the currency concerned is fixed, but there also exists, simultaneously, statutory regulation of the whole, and not merely a part, of the volume of fiduciary issue, either in respect of the proportion of reserve backing to be maintained, or with reference to the legal maximum of issue. The Indian position, in effect, amounted to leaving the total volume of currency in circulation unregulated, in itself, while merely fixing the exchange value of the rupee. On occasions, when the latter was not fixed, by virtue of its control over the volume of currency, the State could make the exchange rate almost what it liked if only it firmly set itself doing it.

The Reserve Bank of India Act does not remove the anomaly of the situation. Under it, the rupee coin continues to be unlimited legal tender and it is obligatory on the part of the Reserve Bank to exchange notes for coins, and vice versa, on demand. The issue of rupee coins requires no reserve backing, nor does there exist any maximum limit as to their issue, and, as before, the monopoly of issue rests with the Government. Only, the Reserve Bank has been made the channel of issuing them to the public. Thus the purely arbitrary element, determining the total quantity of money, persists.

§ 22. The only change has been the placing of one part of the fiduciary issue on the proportional reserve system basis. The old system based on the British model, whatever its virtues in respect of an international financial centre, where the prevention of a multiple contraction of currency on the export of a given quantity of gold should be the greater concern, was wholly unsuited to a dominantly agricultural economy, like that of India, with no alien fugitive balances to provide against, in the event of their taking to wings, and where elasticity of currency supply was the more important factor. It was thus a measure of reform long overdue.

But mere statutory provision for elasticity is not enough ground for optimism regarding the smoothing out of the chronic seasonal fluctuation in the money rates. It is important that the increased issue of paper currency during periods of business activity should not be neutralised

in its effects on the total volume of currency, and, therefore, on the money rates, by an equivalent contraction in the issue of rupee coins. There should be available an adequate supply of eligible bills of exchange and promissory notes, additional to issue notes against, and the proportion of the reserves should be sufficiently in excess of the legal minimum.

§ 23. **Sterling exchange standard.**—The Act puts the rupee on a sterling exchange standard. It makes it obligatory on the Bank to buy and to sell sterling for rupees in unlimited amounts, at the upper- and the lower-sterling points, which, unlike in the 1927 currency Act, are statutorily fixed at $18\frac{3}{16}d.$ and $17\frac{49}{64}d.$, a rupee, respectively. The Indian Legislature, under the new constitution, would not be competent to consider any amendments to this Act, except with the consent of the Governor-General. It has been provided, however, that when the international monetary position becomes sufficiently clear and stable to make it possible to determine what will be suitable as a permanent basis for the Indian monetary standard, the Bank should report its views on the subject to the Governor-General. Sterling, no doubt, will then have returned to gold, and the Board of Directors are bound to be of opinion, that, sterling being as good as gold, the rupee would have all the advantages of a gold standard by continuing to be on sterling; at the same time, it would enable investment of currency reserves in interest-earning sterling securities instead of in gold. The Governor-General, on his part, would see no reason to disagree with the Board, and the rupee, as ever, would continue on sterling.

§ 24. The Bank is required to make public, from time to time, the standard rate at which it would be prepared to buy or to re-discount, bills of exchange or other commercial paper, eligible for the purpose, under the Act. The development of a bill market in India would depend upon whether the bank rate was above or below the market rate. The British practice would seem to be unsuited, from this standpoint, to Indian conditions. It was found to be so in the

case of South Africa. In France, and certain other continental countries, although, at first sight, it might appear that the British practice was in force, in practice, the American system holds true. If the bank rate is below the market rate, bill finance will receive a bounty and, as was the case in America, an adequate bill market may be expected rapidly to spring up in India. Otherwise, however much we may desire one, the chances of success would seem to be few.

§ 25. **Agricultural Credit Department.**—The so-called Agricultural Credit Department has little in common with the Rural Credits Department of the Commonwealth Bank of Australia, except the name. The Department is only required to maintain an expert staff to "study all questions of agricultural credit and be available for consultation" by the Central, the Provincial, and the Local Governments. It would thus be a research bureau. In addition, the expert staff would "co-ordinate the operations of the Bank in connection with agricultural credit and its relations with provincial co-operative banks and any other banks or organisations engaged in the business of agricultural credit." Thus, it is a separate department engaged actively in the finance of agricultural operations.

This contrasts with the Rural Credits Department of the Commonwealth Bank. It attends to the short term and intermediate credit requirement of the agriculturists and the rural industries, their long-term loan requirements being attended to by the four State Agricultural Banks. The Department provides credit to finance the harvesting, processing and movement of crops, and their marketing. The advances made are to be repaid within a year, and all engaged in the production of primary produce (which term is so defined as to include wool, grain, butter, cheese, fresh, preserved or dried fruits, cotton, sugar, etc.) are eligible for the benefit. The Bank does not deal with individuals but only with corporations like agricultural societies or unions. The total advances made by the Department amounted to £45·2 millions by 1932.

The rate of interest charged has varied between 6½ per cent. and 4¾ per cent. The Bank is authorised to issue debentures for the benefit of the Department, borrow from the Treasury up to £3 millions, and 25 per cent of the profit of note issue accrues to the Department until the total reached £2 millions. This limit was reached in 1932. Far from involving the Bank in losses, the Department showed a profit of £350,000 by the end of 1933.

§ 26. **Inauguration of the Bank.**—The Bank was officially inaugurated on April 1, 1935. To begin with, however, it took over merely the control of the Issue Department and the management of the banking business of the Government. The first statement of its accounts was for the week ended May 5, 1935. Much of the time in the first few months of its career was taken up by the necessary preliminaries of organization and the framing of the Regulations under terms of section 58 of the Reserve Bank of India Act.

On May 5, 1935, it established official contact with the member banks, by accepting their statutory deposits under section 42 of the Act. It also announced at the same time (4th July) the first official bank rate (3½ per cent) in terms of section 49. The materials on which to adjudge the working, the progress, and the policy of the Bank, comprise the weekly balance sheets, the monthly summary of statistics, the report of the annual meeting of the shareholders, the annual report on currency and finance, the bulletins issued by the Agricultural Credit Department, periodical circular letters to various bodies, and the statutory report submitted in 1937 under section 55 (1) of the Reserve Bank Act.

§ 27. **Sterling remittances.**—These reveal that, since its inauguration, the activities of the Bank have been steadily growing, although it is far from having approached its full stature yet. It has discharged with distinct success its responsibility of maintaining the stability of the external value of the rupee, its obligation to meet the exchange

requirements of the Government, both of which are closely related, and its duties as bankers to the Government generally. The first three years presented no difficulty whatever in obtaining the sterling wants of the Government. For this purpose, following the traditional policy of the Secretary of State which was later adopted by the Finance Department of the Government of India, it purchases sterling by weekly tenders from the scheduled banks and between the tender dates, "intermediates" on tap at $\frac{1}{32}d.$ above the latest tender rate. Owing to the steadiness of the rupee-sterling exchange, which was largely due to the continued improvement in the terms of trade, the Bank was able to buy sterling at 1*s.* $6\frac{1}{8}d.$ as also to effect occasional intermediate purchases at 1*s.* $6\frac{5}{32}d.$ Besides meeting in full the demands of the Government (Rs. 35·6 crores in 1935–36, Rs. 54·8 crores in 1936–37, and Rs. 49·6 crores in 1937–38), the Bank was able to augment its sterling assets in the Issue Department from Rs. 48·63 crores in April, 1935, to Rs. 80·3 crores in December, 1937.

In April, 1938, however, owing to the continued decline in the favourable trade balance, the market was weak and there was a fall in the sterling tenders. The Bank reduced its tender rate to 1*s.* $6\frac{3}{32}d.$ only to find that this was immediately followed by a decline in the market rates. At this stage it was obvious that the best policy was to withdraw from the market and the Bank altogether suspended its purchases by tender in the beginning of May. In June and the succeeding months improvement in the surplus exports steadied the market once again and the Bank was able to purchase intermediates in July, 1938, and the following months. But the total amount of sterling bought in 1938 (£19,058,000) was insufficient to meet Government's remittances on account of Home Charges. It was, therefore, supplemented by £15,605,000 worth of sterling securities from the Issue Department. In the first instance they were transferred to the Banking Department against an equivalent contraction of its cash balances and were finally handed over to the Government in exchange for payment out of revenues.

In substance the process had the same effect upon the reserves and the circulation as when the Secretary of State drew upon the Paper Currency Reserve in London and the Government transferred to the same fund in India from out of its revenues or, in a direct gold standard country, gold was bought from the Central Bank for export in liquidation of its passive balance of payments. But the Bank was able to increase its sterling securities in the Issue Department in the first half of February, 1939, and to resume sterling purchases by tender in the first week of March. The market, however, soon weakened again and except for the first tender which was heavily oversubscribed, the response was not promising. In May the Bank rejected all the tenders which were at 1*s.* $5\frac{29}{32}$*d.* and withdrew from the market, which it has not re-entered as yet (June, 1939). The Bank has thus been faithfully pursuing the exchange policy of its predecessor, the Finance Department of the Government of India, with equal success.

§ 28. **Bankers to the Government.**—It has assumed practically all its duties and responsibilities as bankers to the Central Government, Provincial Governments, and the Government of Burma. The Bank accepts monies for their account, manages the public debt, and floats their loans and treasury bills. Since the inauguration of the new constitution in the Provinces, the latter maintain separate accounts with the Bank. In return for the various services rendered, they have to maintain certain minimum balances with it and have to cover any temporary deficits in the balances by borrowing on ways and means account from the Bank or issuing their own treasury bills. Several Provinces have taken advantage of the new powers of borrowing conferred upon them by the constitution and in 1937 and 1938 five Provinces floated loans through the Bank of an aggregate amount of Rs. 710 lakhs. In 1938 four Provincial Governments issued their own treasury bills and the Bank also made ways and means advances to some to cover the shortage in their minimum balances.

It has always placed its best advice at the disposal of

the Governments, Central as well as Provincial, who have shown appreciation of its services in this respect by consulting it on all matters relating to banking. The Bank assisted in the formulation of a scheme of sinking funds for the debentures of land mortgage banks. It gave its opinion on the various measures relating to agricultural debt and in 1936 it was consulted and gave its opinion on the amendment to the Indian Companies Act, chiefly that portion of it which related to banking companies. Several Provincial Governments have taken advantage of the consultative and advisory services of the Agricultural Credit Department of the Bank for a solution of the problems facing the Co-operative movement.

§ 29. **Bankers' Bank.**—In the sphere of its relation with the member banks and the money market generally, however, no spectacular successes mark the record of the Bank. It is still evolving its own organization and it does not seem to have travelled far beyond the stage of establishing contacts. It has five offices of the Banking Department, one each at Bombay, Calcutta, Delhi, Madras, and Rangoon, and seven branches of the Issue Department, one each at Bombay, Calcutta, Cawnpore, Karachi, Lahore, Madras, and Rangoon. The Bank has also an office in London. Besides through its own branches it can reach all parts of the country through over 350 branches and offices of the Imperial Bank of India.

When the Bank commenced business the number of the scheduled banks was 48, which included the Imperial Bank of India, 19 Exchange Banks, and 28 Indian Joint Stock Banks. In December, 1938, their number rose to 57, on account of an increase in the number of the Indian banks from 28 to 37. The increase in membership represented an increase in the aggregate current and time liabilities of the scheduled banks from Rs. 208 crores to Rs. 239 crores. If we exclude the indigenous bankers, the member banks of the Reserve Bank would represent the major part of the banking strength of the country. The statutory deposits maintained by them with the Reserve Bank, as a glance

at the balance sheet of the Banking Department will show, form by far the largest portion of the Bank's working capital. The statement dated June 2, 1939, for example, shows that out of a total deposit of Rs. 26·06 crores, the member bank deposits were Rs. 13·78 crores.

§ 30. **The Bill market.**—In the four years of its career the organization of the Indian money market has not shown any considerable improvement. The Bank has not been able to stimulate the development of a bill market. On the contrary, the magnitude of the finance through bills has appreciably suffered after the commencement of the Bank. The bill portfolio of the scheduled banks fell from 2·5 per cent of their demand and time liabilities in 1937 to 1·5 per cent in 1938. The corresponding percentage for the banks in Great Britain usually ranges between 10 to 15 per cent. The absence of a well organized open bill market where first class bills can be freely negotiated and through which Central Banks can enforce their credit policy, deprives the Reserve Bank of India of any effective grip over the market. It has necessarily to restrict its operations to the market for gilt-edged securities.

The growing unpopularity of bill finance and the preference for cash credit finance, in part, no doubt, follows the world trend. But there are special reasons why the bill should take readily to the Indian soil. The system of branch banking is not so well developed in India as in some European countries to make the more elastic and tax free letter of credit equally attractive and the bill is a very ancient institution in India, which is quite familiar to the businessmen and financiers of the country. The balance of advantage, therefore, seems capable of being shifted in favour of the bill.

The statutory report of the Reserve Bank recognises that the ultimate solution for the ineffective central bank control over the component parts of the market must be in the development of an open bill market. But it apportions the blame for the decline of the bill between two chief factors. First, the cheapness of money makes a free market

even in treasury bills unprofitable, so that the marketing of trade bills with marginally less security affords even less prospect of success. Secondly, the rates of stamp duty, 9 as. per cent *ad valorem*, which may not possibly be inappropriate at times of high interest, now impose what is practically a prohibitory tariff on this form of document.[1]

To these explanations must be added a third one, which is at least as important as the first two, namely, the rate structure of the money market, the influence of which on the market for bills has been referred to elsewhere in some detail. The Reserve Bank rate, i.e., the rate at which the Bank is prepared to buy or rediscount bills of exchange or other commercial paper eligible for purchase under the Act has throughout the period been identical with the Imperial Bank *hundi* rate, which is the rate at which the Imperial Bank is prepared to discount first class three months' bills. Both remained at 3½ per cent until November, 1935, when they were brought down to 3 per cent. The market rate for bank loans has throughout been appreciably lower than the official rate: bank loans have been freely granted at less than 2 per cent. This offers no inducement to the banks to encourage bill finance.

§ 31. **Indigeneous bill market.**—Also the indigenous bill market, i.e., the market for bills drawn by or on the indigenous bankers must, under the terms of the Reserve Bank Act on the one hand and the prevailing unwillingness of the bankers to change their old methods of business on the other, remain beyond the ambit of the Reserve Bank. For most of their working capital they depend upon their personal or family resources and usually they are their own mutual lenders of last resort, so that they form more or less a separate organization, distinct from the rest of the market. Their borrowing from the joint stock banks is not on a sufficiently large scale to make them necessarily dependent upon the credit policy of the banks, and through the latter upon the credit policy of the Reserve Bank. They are responsible for financing most of the inland trade and

[1] Report (1937), pp. 43–44.

industries and the *hundi* constitutes the largest part of the internal bills.

No scheme for stimulating a discount market, therefore, is likely to be fruitful, if the private banker is left out of account. At the same time, unless the bankers are agreeable to shed their non-banking business, maintain proper books of account, periodically publish properly audited balance sheets, and accept the conditions for inclusion in the bank's schedule, member bank privileges of discount cannot be extended to them. Negotiation on the part of the Reserve Bank, which fully appreciates the importance of the indigenous bankers, with representatives of the latter, was not fruitful. The provisions of the Companies Act, which make penal the mixing of other forms of business with banking after January 15, 1939, for all firms bearing the name 'bank', however, may possibly have some indirect influence upon such bankers as may wish to use the name.

Thus the old division between what have come to be termed the European and the Indigenous parts of the money market persists. The Reserve Bank has not been able to bring about their fusion. At present the banking structure of the country falls into three broad groups: the scheduled banks, the non-scheduled banks, and the indigenous bankers. The contact of the Reserve Bank with the first group, which is statutorily provided for, though still not sufficiently close, nevertheless is closer than with the rest. Most of the non-scheduled banks have borrowing relations with one or other of the scheduled banks. Indirectly, therefore, through its hold upon the member banks the Reserve Bank can hope to influence the policy of the non-scheduled banks. The Bank has also made independent efforts to get into direct touch with them. In November, 1938, it addressed a circular letter to about 300 of them having a capital and reserve of Rs. 50,000 or over, to enquire whether they would be willing to keep in touch with the Bank for advice and guidance. But the Bank has hardly any control over the indigenous bankers.

§ 32. **Control over the money market.**—Cheap money conditions, in common with the outside world, having generally persisted throughout the four years under review, it is difficult correctly to assess the influence and the control of the Reserve Bank over the scheduled banks and the market generally. There has not arisen any occasion for testing the ability of the Bank to induce changes in the market rates of interest upward or downward. The situation has been almost wholly dominated by such plentiful supplies of short-term money as to be nearly unlendable on occasions. For example, it is not possible to say how far the absence of the customary seasonal fluctuation in the official rate during the period has been due to the policy of the Reserve Bank or whether it merely reflected the prevailing market conditions. For, the Bank rate (the Imperial Bank *hundi* rate) remained steady since the middle of February, 1933, i.e., for over two years before the coming of the Reserve Bank.

§ 33. Also the amplitude of the seasonal variation in the note issue of the Bank has not shown any appreciable difference in the post- as compared with the pre- Reserve Bank period. The following table gives figures of the highest and the lowest amount of the issue for each year from 1932 to 1939.

Gross Note Circulation

(in crores of rupees)

Year	A *Highest*	B *Lowest*	*Difference between A and B*
1932	180	168	12
1933	180	174	6
1934	186	177	9
1935	195	184	11
1936	203	194	9
1937	214	207	7
1938	216	208	8

It would seem difficult, therefore, to attribute the steadiness in the rate to the currency policy of the Reserve Bank with regard to the seasonal variations in the volume of issue. The range of variation in the issue being no larger than before, one might as well argue that the rate would have remained steady even if the old system had continued, as indeed was the case for two years before the inauguration of the Reserve Bank.

§ 34. Though the official bank rate has remained steady, the other rates, with the exception of the Imperial Bank *hundi* rate, have not done so. The inter-bank call rate and the bazaar *hundi* rate have constantly fluctuated. The former (in Bombay) has varied between $3\frac{1}{2}$ per cent and $\frac{1}{4}$ per cent and the latter between 8 and 5 per cent in Calcutta and between $6\frac{3}{4}$ per cent and 3 per cent in Bombay. A probable explanation seems to be that the scheduled banks when in want of temporary accommodation find it less expensive to take recourse to the call market rather than approach the Reserve Bank for funds. Similarly, the bazaar depends upon mutual borrowing for emergency money. That is to say, neither bazaar nor the market is effectively linked with the Reserve Bank. The same applies to the money rates as between the several money centres in the country. The difference between the call rates as between Calcutta and Bombay has frequently been as much as $\frac{1}{2}$, $\frac{3}{4}$, or even $1\frac{1}{4}$ per cent. And the banks' (fixed) deposit rates in the two centres often differ by a much wider margin.

§ 35. **Lender of the last resort.**—As a lender of last resort, theoretically, the Reserve Bank is willing at all times to re-discount for the scheduled banks approved bills bearing their signature at the official rate. In practice, however, the bills discounted by the bank did not at any time exceed Rs. 288,000 (May, 1937). It did not issue any currency against "Internal Bills of Exchange and other commercial paper" which is an item on the Assets side of the Issue Department of the Bank. Advances to member banks on the pledge of approved securities are also negligible, though appreciably more than the Bank's discounts. The advances

of Rs. 2·09 lacs made in April, 1939, is exceptional. Otherwise the highest aggregate of advances to member banks was Rs. 22·85 lacs (September, 1937). The maximum for 1936 was Rs. 2·63 lacs (April), for 1938 Rs. 1·30 lacs (May), and in the first half of 1939 no advances were made to member banks.

§ 36. The coming of the Reserve Bank has not meant any great change in the number of bank failures, which has always been a regular feature of banking in India. But it must be said at once that nothing can, probably, save the great majority of them. Their capital structure is meagre, they do not follow any accepted banking ratios with regard to cash, deposits, advances, and investments, and unless they abide by the well tried canons of commercial banking a Central Bank cannot usefully come to their rescue. But the banking crisis towards the close of June, 1938, which came as a sequel to the failure of the Travancore National and Quilon Bank (a member bank with a capital and reserve of about Rs. 30 lacs and 81 branches), revealed the absence of close relations between the scheduled banks and the member banks. The crisis induced the Bank to issue a circular letter to the latter, laying down the procedure to be followed for obtaining advances from the Bank, and its officials, for the first time, established informal contacts with South Indian scheduled banks through visits. But the existing law does not arm the Bank with any powers of control over the banking system of the country beyond the reserve requirements of the member banks. It is possible, however, that the recent representation made by the Bank to the Government may lead to a comprehensive Banking Act which may seek to remedy the present deficiencies.

§ 37. **Agricultural Credit Department.**—The Agricultural Credit Department is engaged in an intensive study of all problems relating to rural finance. The results of its researches are made available to the public, from time to time, in the form of bulletins. So far four bulletins have been issued. The first gives an account of the (co-operative)

Banking Union in a taluqua in Baroda State, the second examines the numerous activities which a village (co-operative) bank should perform, the third is a report on the development of co-operation in Burma, and the fourth deals with the progress of co-operation in a village in Punjab.

By section 55 (1) of the Reserve Bank Act, the Bank was required to make a report to the Central Government within three years of its inauguration on (*a*) the extension of the provisions of the Act relating to scheduled banks to non-scheduled banks and bankers and (*b*) the improvement of the machinery for dealing with agricultural finance and the methods for effecting a closer connection between agricultural enterprise and the operations of the Bank. Towards the close of 1936 the Bank issued an interim report on agricultural credit which was followed in December, 1937, by a final report. Like the bulletins issued by the Agricultural Credit Department, the report has proved to be primarily educative and advisory in its purpose. It makes no concrete proposals for legislation with regard to indigenous bankers as the negotiations between the two parties fell through. On the subject of agricultural credit the report explained the inadvisability of a central bank, whose advances and investments must be highly liquid, engaging in agricultural finance. It endeavours to allay the wrong impression, widely entertained, that the Department was meant to extend credit to agriculture. The report, in effect, makes it clear that it is only a research department.

§ 38. **Conclusion.**—Thus, while the Reserve Bank of India seems to have done eminently well in those spheres of activities where its predecessor the Finance Department of the Government of India (in co-operation with the Imperial Bank) had functioned satisfactorily, it does not seem as yet to have strikingly triumphed in those others in which the old system was generally recognised to be deficient.

CHAPTER XXXI

RECENT TRENDS OF INDIAN PRICES

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I

The nature of price statistics.—A study of the prices in India with the available statistics is not very easy. While the index numbers of wholesale prices for Calcutta and Bombay are quite local in character, the index number for India has outlived its usefulness. Here the base year is 1873, to which India no longer looks back with any interest. Between 1873 and 1937 the whole economic framework of India has changed. The outlook of the people has altered. The relative importance of commodities in Indian trade and industry has changed appreciably. The statistics at our disposal are therefore not adequate for any reliable conclusion.

Under the circumstances the index number of wholesale prices in Calcutta has been accepted as the second best guide. The League of Nations has accepted it for all comparative studies. Even the all-India price index is nothing but a Calcutta index and not really all-India in character. Nearly four-fifths of its price quotations are from this city, for when the framework of this index was prepared the seat of the Imperial Government was in Calcutta. Besides, since 1925 the wholesale price index of Calcutta has closely followed the movements of the all-India price index. Calcutta may not represent the economic condition of the country as a whole—for which one is to look to the Indian villages differing among themselves in social structure and economic character—but it is one of the two centres of trade and industry where major economic changes cast their reflection. The object of studying changes in the general level

of prices is to establish relation between currency and exchange and to know its effect upon production and distribution. Calcutta, along with Bombay, is an important centre of Indian trade and industry and all important markets are situated here. It is linked up with the markets of the world. The Calcutta index can, therefore, be relied upon for our purpose. For knowing the effect of currency and exchange upon price, and of prices upon the major industries of the country, upon industrial wages and profits, it will be sufficient. But a study of the economic dynamics of Indian villages, of real India, will always remain a baffling problem for want of data.

Index Numbers of Wholesale Prices in India

[(c) and (d) have been shifted to the base 1940 = 100]

	Calcutta weighted, 72 articles (a)	*Bombay 40 articles (b)*	*India unweighted, 39 articles (c)*	*India weighted, 100 articles (d)*
1914. .	100	100	100	100
1920. .	201	216	191	161
1921. .	178	198	161	146
1922. .	176	187	158	142
1923. .	172	181	146	139
1924. .	173	182	150	137
1925. .	159	163	154	142
1926. .	148	149	147	139
1927. .	148	147	137	138
1928. .	145	146	137	139
1929. .	141	145	138	136
1930. .	116	126	116	114
1931. .	96	109	86	84
1932. .	91	109	86	80
1933. .	87	98	82	74
1934. .	89	95	81	73
1935. .	91	99	86	80
1936. .	91	96	—	—
March, 1937	100	—	—	—

II

Post-War price changes.—Since the War the Indian price level was moving up due to the abnormal factors caused by it. The upward movement gained impetus after the War and prices were soaring up. The price level attained its peak in 1920 till when war conditions were prevailing. From 1921 onwards nations were busy with reconstruction and rehabilitation. In that year the price level came down very low. Till 1924 prices continued to decline rather slowly. In 1925 and 1926 there were again two sudden set-backs. By this time it appeared as if prices had settled down to a new normal. From 1926 to 1929 prices were relatively stable, their behaviour was normal, and the disparity between them eased up. This condition did not continue long. The great economic depression commenced from 1929, the like of which had never been witnessed before. India became a victim to it. The price level came down precipitously in 1929 and 1930 and was further declining rapidly to a ruinous level. The Calcutta index shows that the price level was at its bottom in 1933 when it recorded 87. In March the record was as low as 82.

The depression is scarcely over. But the price level has taken an upward turn. It was slowly moving up after March, 1933, reaching 91 in 1935, where it remained in 1936. It appeared that the prices had attained a new level. By the end of 1936, however, the political situation in Europe took a new turn. Nations were adopting a hasty and drastic policy of rearmament. The war scare fanned up speculative spirit and the price level rapidly shot up, when by March, 1937, it reached the pre-war level.

On two occasions after the War the fall in the general price level was very sudden and precipitous. The effects were not, however, the same. The fall of 1921 and the succeeding years was amply compensated out of the war-time artificial profits. A part of the burden was subsequently shifted to the wage-earners and rentiers, who were more than compensated by the relief obtained

through the fall of price level. This fall was at the same time accompanied by an all-round reconstruction programme, throwing open to capital and labour new avenues of remunerative employment. The general purchasing power was distributed over a wider field of consumption and production. This fall was not associated with a period of depression and unemployment of the factors of production. It was associated with an industrial boom along different channels.

During the period of relatively stable price level between 1925 and 1928, the remuneration of the factors of production attained a new level which settled about the margin. The fall of the price level in 1929 therefore worked differently. It told heavily upon the margin of remuneration, without lending any scope for fresh employment elsewhere to the different factors of production. The rates of profits and wages were so low that the factors of production could not accept them. This caused unemployment of labour and capital. Unemployment of labour or contraction of income below the normal requirements of the owner is vicious in its consequences. It causes contraction of consumption and a further fall of price level.

Looking back over the last twenty-three years, it is very difficult to extricate the normal behaviour of the Indian price level out of its erratic movements. Between 1914 and 1937, only four or five years looked free from abnormal factors. A very large number of years witnessed an abnormal behaviour of economic forces. Even those few years which found relatively stable price levels were not tested by time so that they could otherwise be accepted for a reliable price study. The depression which followed immediately after this period proved that the economic conditions of the period were without any basic solidarity. The economic forces, internal and external, did not attain any equilibrium. Nevertheless, the period between 1926 and 1928 has been accepted as a new normal by a large number of countries. There is no justification for that. Pre-war normality might have lost its basic foundations, but no new base has been found out. The price level is floating about without any anchor.

III

Currency policy and prices.—During the years of trade and currency dislocation caused by the War, there was little uniformity in the movement of prices in different countries of the world. Currency and exchange were dislocated. They depreciated in various degrees in different countries. Difficulties of communication and transport, instability and uncertainty of exchange, and the existence of tariff walls along national frontiers hampered trade. There was no free competition. Restoration of equilibrium proved difficult. Prices followed incoherent courses. They became almost national in character by being influenced largely by national policies. There was no uniformity among the price indices themselves nor among their tendencies.

When in the years following 1925 several countries were returning to the gold standard one after another, national economic policies were regulated to conform with international equilibrium. National prices showed tendencies to follow international prices. This necessitated an attempt to make an artificial readjustment of several important national factors. The readjustments were forced upon them indirectly by currency and trade regulations rather than directly by any coherent plan. The outward manifestation of price level became relatively steady, but the fundamental factors which ultimately control price structure were weakened. There were elements of instability in them. National economic equilibrium became disturbed. It could not be accepted as fully reflecting the economic conditions in the country concerned.

The Government of India followed a similar policy. They tried to attain a level of equilibrium with sterling in an artificial manner. In their attempts to stabilise the rupee at 1*s.* 6*d.*, a policy of deflation was followed. In the words of Sir Purushottamdas Thakurdas, a trenchant critic of this policy of the Government, while the pre-war average expansion of currency in India was over Rs. 20 crores per annum, the average expansion between 1921–22 and 1924–25

was Rs. 11·12 crores a year. To proceed with this calculation, between 1924–25 and 1928–29, the annual average expansion was Rs. 4·8 crores. The Bank rate was naturally high during this period; wages were relatively burdensome; but the price level declined. The fall was not followed by any adjustment in the internal economic factors.

The Government of India, however, attained their objective. During these years of economic and financial reorganisation, Indian price level very closely followed the wholesale price movement in Great Britain. Between 1924 and 1929 the Board of Trade index declined by over 17 per cent and the Calcutta index recorded a fall of over 18 per cent. This downward movement was steady and tenacious. It was much more depressing than in the principal countries with which India had important trade relations, except Japan, where the fall was about 19 per cent. During this period the United States Bureau of Trade index fell by 3 per cent, and the German official index and the French index remained steady.

Nevertheless, it was maintained, for example, in the Majority Report of the Hilton-Young Commission, that the Indian prices were adjusted, by the time India had been returning to a gold parity, with the world prices. The Commission proved this by converting the rupee prices into gold prices in accordance with the gold exchange of the rupee. This, however, does not throw any new light on the problem of international competition in trade and production when the price index is not a true index of the adjustment of internal factors of production which constitute cost. Such a calculation merely begs the question that foreign exchange is the ratio between two price levels, so that when the national price level is converted into a foreign price level in terms of the current ratio of foreign exchange, even when exchange is varying, a parallel movement of the two prices will be observed. It supports the claim that the regulation of the Indian exchange by the Government was very effective. It proves that the regulation of exchange had its complete effect upon prices without proving in the least how far it brought similar

adjustment of wages, rent or interest to suit the declining price level. It is to be remembered that the rupee exchange was adjusted with sterling and sterling with gold at an artificially high level unwarranted by the economic and financial condition of Great Britain. Great Britain suffered and India suffered in consequence. A precipitate fall of the Indian price level proved ruinous to India.

IV

National and international price movements.—The object of comparing national price level with international prices is to compare the competitive position of different countries. For this purpose Indian prices require comparison with the price levels in the United Kingdom, Japan, the U.S.A., Germany and France. With these countries India has important trade relations. This end is, however, rendered unnecessary by the state of price depression to an unprecedented extent. Price levels in several countries declined to such an extent that it was the upward movement which was desired while the downward tendency was regretted. When the depression brought down the purchasing power of the people to a very low level, even a very great price depression could not bring down a long list of commodities within the range of consumers' or producers' demand. Even low price would not introduce elasticity into the demand. On the other hand, the cost structure proved too rigid to follow the price depression. Consequently, unprofitable productive effort further aggravated the situation. Nations, therefore, desired not competitive advantage in international trade under falling prices, but profitable enterprise under rising price level; and thus an increase in employment and the general purchasing power of the people.

During the period of price depression since 1929, the structure of Indian prices revealed its inherent weakness in comparison with the price level in other countries. In the disparity of prices which ensued, Indian prices diverged away to an extremely low depth. This divergence became

very prominent since 1931 from when one country after another was raising its anchor off gold. Between 1929 and 1931, measured in national currencies, the price level fell in Japan by 30 per cent, in the United Kingdom by 23 per cent, in the U.S.A. by 23, in France by 20, and in Germany by 12. The Indian price level, however, fell to the extent of 32 per cent without bringing any relative advantage to trade. From 1931 price movement, in those countries which left the gold standard either openly or practically and which depreciated their currencies in terms of gold, became relatively steady; the decline was stopped and after a year or two there ensued an upward movement in certain countries. Japan checked the fall in price level in 1931, the United Kingdom in 1932 and Germany in 1933. India, however, proved an exception. Immediately after India had left gold, the general price level reacted to the new measure. Between September and December, 1931, the index number of prices moved up from 91 to 98. With 1932 all hopes of price revival were shattered. Indian prices went down to the lowest level of 82 in March, 1933. The annual average price level remained tenaciously low for several years, although the downward movement was checked in 1933. The general price level did not go up very much higher than where it had been checked till the advent of 1937. While the year 1935 was a year of definitely rising prices everywhere except in the gold bloc, and while the price disparity among most countries was closing up, Indian prices remained depressed and furthest away from the world movement.

Index Numbers of Wholesale Prices

(shifted to the base, 1929 = 100)

	Calcutta	*Japan*	*U K.*	*U.S.A.*	*France*	*Germany*
1929	100	100	100	100	100	100
1930	82	82	88	91	88	91
1931	68	70	77	77	80	81
1932	65	73	75	68	68	70
1933	62	82	75	69	64	68
1934	63	81	77	79	60	72
1935	65	84	79	84	54	74

V

Wholesale and retail prices.—"The years of depression had witnessed—were, indeed, largely caused by—a profound distortion in the structure of prices; wholesale prices fell much more than the cost of living, raw materials more than the manufactured goods, farm products more than the industrial products, consumption goods more than investment goods. As a result of these divergent movements, the balance of economic relationship between producers and consumers and between different classes of producers was destroyed and a long-jam developed which prevented the movement of goods and generation of purchasing power. Since 1933 . . . there has been a well-marked tendency in many parts of the world towards better price relationships. In most cases, this has been the result of a considerable rise in the prices of those commodity groups which fell most during the depression, accompanied by relative stability in the prices of those groups which fell least. In other words, in revival as in depression, the movement of prices has tended to pivot around those prices which are relatively inflexible."

In these words the Director of the Financial Section and Economic Intelligence Service of the League of Nations gives his survey of the inequalities in recent price movements. In certain respects India proved no exception to this trend, in others India maintained her own peculiarity.

In most countries of the West retail prices as measured by the cost of living index proved relatively rigid. Wholesale prices fell much more relatively to retail prices. A relatively rigid cost of living did not encourage extension of demand in spite of a greater fall in the wholesale prices. This helped to prolong the depression. In India, however, the retail prices fell more than the wholesale prices or at least kept pace with them.

When the cost of living is rigid, a fall in the wholesale prices does not cause the demand to expand and the margin of profit of the trader and producer is narrowed down. If wages keep pace with the cost of living, manufacture as

Index Numbers of Wholesale and Retail Prices[1]

(Shifted to the base, 1929 = 100)

	Bombay wholesale price index (*a*)	*Bombay cost of living index* (*b*)	*Wholesale prices of cereals, Calcutta, 8 commodities* (*c*)	*Retail prices of cereals, India, 7 commodities* (*d*)
1929	100	100	100	100
1930	87	92	80	70
1931	75	74	62	46
1932	75	73	54	51
1933	68	69	53	49
1934	66	65	55	48
1935	68	68	60	51
1936	67	68	63	—

well becomes less profitable. The wage-earners' position remains unaltered so far as it is related to these factors, while the position of the manufacturers and traders remains depressed. When retail prices fall more than the wholesale prices, as was sometimes the case in India, profits of the retailers are narrowed down. As channels of bringing the demand of the consumers to the door of the wholesalers and manufacturers, these retailers lose their incentive. But with the decline of the cost of living, people with fixed income profit and wealth tends to be transferred to their hands, provided other factors remain the same. If wages move along with the cost of living, one of the burdens of the producers is minimised. In fact, however, wages lag far behind the cost of living. In a system of production like that of India, where it is less capitalistic, the commodities being agricultural produce, a relatively greater fall of retail prices, as was the case with cereals in particular, is suicidal for both trade and production, for both are almost combined in the same hands. In this respect there are very little signs of improvement even now. The very fact that in India the retail prices have

[1] Calcutta cost of living index is not available. Hence Bombay figure has been taken. The last two columns of figures have been put together from two different sources and hence are not comparable.

fallen much lower than the wholesale prices is another proof of the existence of certain factors which are peculiarly Indian; for wholesale prices are generally influenced by world factors more than the retail prices.

VI

Distortion of the price structure.—One of the characteristic features of the price depression since 1929 is, as has already been said, the disparity between the price levels of raw materials and manufactured commodities. Among the raw materials, staple agricultural commodities suffered most. This can be seen by a glance at the movement of prices of exported and imported articles; for the former consist mostly of raw materials and the latter of manufactured commodities.

	Indian Index Number series, 1873 = 100		*Calcutta Index Number series*, 1914 = 100	
	Exported articles	*Imported articles*	*Exported articles*	*Imported articles*
Sept., 1929	217 = 100	167 = 100	133 = 100	150 = 100
Dec., 1931	123 = 57	145 = 87	81 = 61	124 = 83
,, 1932	120 = 56	129 = 77	69 = 52	115 = 77
,, 1933	114 = 53	125 = 75	73 = 55	112 = 75
,, 1934	124 = 57	124 = 74	76 = 57	109 = 73
,, 1935	— —	— —	85 = 64	109 = 73
,, 1936	— —	— —	82 = 62	105 = 70

It will be seen that the fall in the price of raw materials as represented by the exported articles was very sudden and great, while the decline in the price of manufactured articles represented by the imported articles was rather slow. By 1934 the prices of manufactured articles had comparatively adjusted themselves to the level of prices for raw materials, while at the same time raw material prices were showing signs of slight improvement.

A relatively greater depression of the prices of raw materials brought no advantage to the manufacturers through lower costs. The malady in the present depression

was lower demand rather than higher costs. Decline in the selling price of staple agricultural commodities weakened the purchasing power of the agriculturists. India being predominantly an agricultural country, the suffering of the people was very great. In the words of Sir George Schuster, "India has felt the severity of the fall in the case of what she has to sell, but has not obtained a corresponding advantage of the fall in prices of what she has to buy." In consequence, prices of manufactured articles had ultimately to come down to the level of primary commodities.

Another approach to the problem of price study is to compare the prices of investment goods with those of consumption goods. During the present depression the prices of the latter have come down much lower than those of the former, thereby raising the cost of production, and making investment unprofitable and discouraging. This is considered to be one of the reasons for the sluggish nature of the recovery. In India such a comparison is fruitless as much as it is difficult. In a capitalistic industrial country where productive activity depends considerably upon the price and cost of capital, this approach to the problem is essential. In India, which is dependent upon agricultural production, overwhelmed with unsaleable crops for want of purchasing power, such an analysis is unnecessary. Neither are the Indian price statistics such as to throw much light on the problem. Nevertheless, it may be said in general that while the price of crops has come down very low, the price of capital goods has not declined to the same extent. A similar disparity will be evident if oil is compared with oil-seeds or if the indexes of metals, hides and skins, building materials, etc., are observed, which are maintaining relatively higher positions. If, however, raw jute is compared with jute manufactures or cotton with cotton textiles, the conclusion will be quite otherwise.

The final measure of the price distortion will be evident from the following measure of average deviation of the price index of 72 commodities in Calcutta from the average index of all commodities. It will be seen that even now there is very little hopeful sign of the dispersion tending to be

narrower. It appears that productive activity will have to settle down to a new structural relationship.

1925—27·74	1928—14·04	1931—18·03	1934—18·78
1926—15·97	1929—15·89	1932—20·57	1935—17·10
1927—15·08	1930—18·04	1933—17·39	1936—18·42

VII

Disparity of individual prices.—So far the study of prices has been confined to the movement of the average of price indices. A further detailed study of the movement of individual commodity prices will show that at no time have price movements been so free from common factors as recently. Independent measures in several parts of the world have influenced individual commodities, making the general price index merely a hotchpotch calculation. This is mainly due to the absence of a common currency standard, fluctuating exchange, trade restrictions and control, and a hundred other measures adopted during the period of depression. This is why in 1934, for example, raw jute index can record 39 and tea 125.

Raw jute was the worst victim of the depression. Its bad days had commenced in 1927, two years before the depression started. The depression merely recorded the Nemesis. Recent upward tendency in the commodity prices has helped the price to be in a better position, but the gain itself is disproportionately low. The recent rise is also due to some extent to the restriction scheme adopted by the Government of Bengal, helped by the weather condition. The deplorable position of jute has made the Bengal ryot and those dependent upon him almost resourceless. This bad state of raw jute is due to a combination of several factors: overproduction, better bargaining position of jute mills, large stocks, and the prevalence of a purely gambling spirit in the jute futures markets of Calcutta.

Commodities like cereals, pulses, oil, etc., have also suffered heavily during the depression. These commodities are almost local in character. They depend largely on

home markets. They have suffered most by the depression and have caused in their turn the depression to continue. Wheat is another commodity the price of which has remained low on account of the competition among exporters, shrinkage of the world market, and poverty at home. The prices of these commodities, except oil-seeds, are yet showing no signs of improvement and they will not perhaps improve until the purchasing power of the people is enhanced by other methods, or they are placed in the world market by improved methods of marketing, or they are brought into new industrial use. Since 1935 oil-seeds have witnessed a comfortable rise. It is an exportable commodity and its rise has been ascribed to the prolonged drought in the Argentine and enhanced industrial demand in the West.

Raw cotton has suffered long. Its price depends as much upon the textile industry at home as upon the demand from Japan. The relation between raw cotton and cotton manufacture is to a large extent similar to the relation between raw jute and jute manufacture. The bargaining position of mill-owners is always strong and the ryots are always at a disadvantageous position in marketing. The boycott of Indian cotton by Japan, upon which the export trade is largely dependent, and the subsequent limitation upon Indian cotton purchase by the Indo-Japanese quota agreement to a depression period level, have prevented the rise of the price. Recently the price level has gone up very much higher due to the war scare and heavy purchases by the mill-owners. The rearmament programme has also stimulated the price of hides and skin to some extent.

The Indian jute industry depends almost entirely upon the foreign market. It is one of the industries which has suffered almost as much as any primary commodity. It is one of the commodities which is open to sudden influences of the season and international political situation. Favourable production of world crops gives an impetus to its demand as grain carriers. The world trade in grains has been considerably reduced during the depression, affecting the price of jute heavily. This has been further aggravated due to the use of mechanical devices for carrying grains in bulk, an attempt

on the part of several countries to find substitutes and imposition of heavy import duties by some countries. The price depression is still continuing. But it has not so badly affected the financial position of the mills. A much heavier decline in the price of raw jute has somewhat maintained the profit of the millowners.

Sugar and cotton manufactures are the two important commodities whose prices have been maintained at a very high position by the tariff duty. Relatively they are the most favoured of all commodities. The trends of their prices are, however, different from those of other commodities. Relatively stable and high, the prices of these commodities are tending to come down slowly, by the expansion of competition at home as a result of the protection, if not by increased efficiency. Tea is another commodity, which, though not helped by any protective policy, is now in a very favoured position. This is largely due to the influence of the International Tea Restriction Scheme. Its position is still improving. On the whole, the key products and the protected industries are now in a much improved position, while primary agricultural commodities are still suffering heavily.

VIII

Consequences of price changes.—The causes which led to the price depression in India are world causes. The burden of heavy public debt consequent upon the War, the impossible reparations imposed upon Germany, rampant economic nationalism and tariff barriers along national frontiers, are some of the causes which originally set into motion the vicious circle of depression.

There are, however, certain causes peculiar to Indian conditions which aggravated the depression and are still preventing recovery. India is an agricultural country. Seventy-two per cent of the people are directly engaged in agriculture and a far larger proportion are dependent upon it. Their income is normally so low that it is hardly sufficient for their urgent necessities. Any further fall in the income of the

people consequent upon any extraneous cause, whatever it may be, leaves the people on the verge of starvation. The repercussion which follows aggravates the whole situation. People die in the midst of plenty. Their only capital, *i.e.*, their labour, is lost to them. Besides, the commodities themselves, bulky, unstandardised, and perishable, cannot expect the best market, nor can they wait for a better market condition. The agriculturists themselves cannot wait for a better price when their needs for purchasing power are urgent.

The consequence of the decline of prices has been untold miseries of the people; particularly of the agriculturists. Their purchasing power has come down remarkably low. Unemployment and poverty are beyond description in the villages. Low purchasing power of the masses has affected the industries. The burden of debt has been heavy and credit has frozen up. Trade and transport have suffered; budgetary equilibrium disturbed; fresh taxation necessitated; and the burden of public debt increased. In the chaos that has ensued contradictory phenomena have been observed—poverty amidst plenty, unemployment on the one hand and unreduced wages on the other; rate of interest low with some but high with others; profit eliminated or very low in certain quarters but relatively high elsewhere, and so on. Yet to-day there is very little sign of this situation easing up.

The general outlook of the people has changed. It can no longer be argued in the orthodox economic manner that the fall of prices is wholly favourable to some and unfavourable to others, although maldistribution of wealth has increased considerably. A fall of prices cannot be looked upon as favourable to wage-earners in general in the face of increasing unemployment. It is not beneficial to creditors even, when credit is wanting and capital is frozen. People can no longer rely on the classical theory of automatic restoration of prices, when a fall does not help expansion of demand, the general purchasing power having fallen so low. Neither can currency and exchange be relied upon to help their restoration. In fact they gave way to the pressure of circumstances. Low rate of interest, low price of primary products and inexhaustible supply of labour

have not been able to bring industries on to a profitable basis in the presence of low demand. The present depression in the Indian prices seems to be extremely tenacious. It is now admitted that it cannot be raised by the free play of economic forces. To a certain extent this is a depression period outlook. At the same time it is also true that if no definite measure be adopted to reverse the downward movement of prices, it will take a very long period for the normal or profitable level to be restored, and in the process several factors of production will suffer considerably. Already they have been great victims. Indians have therefore demanded certain remedial measures from the State largely in tune with the Western economic thinkers of to-day. Lowering the burden of taxation, "regulation of exchange," "controlled inflation," "loan expenditure," "planned economy" are some of the measures demanded in India. Of these, the demand for devaluating the rupee-sterling exchange has been particularly strong. The claim for it has been pushed to such an extent that it has now become a plank in party politics. A rapid survey of the thoughts on these demands will be interesting.

IX

Demand for remedial measures.—Several years before the effect of the price depression was being felt, the Indian business community were blaming the currency policy of the Government which stabilised the rupee-sterling ratio at 1*s.* 6*d.* to the rupee. When the price depression commenced the business people as well as the politicians traced it to this exchange ratio. They not only tried to show that the ratio was artificial but also maintained that it offered unwarranted advantage to the foreign industries, caused a serious set-back to Indian industries, reduced the purchasing power of the people, compelled the Government to borrow beyond their necessities in India in order to maintain higher exchange and helped the rate of interest to remain at a high level. The Government of India were termed a "distress borrower" in the Indian money market. "A distress borrower is

uninfluenced by the return on the actual current investments and tends to squeeze out the genuine borrower from the money market." The business community therefore wanted a change in the exchange ratio, which would revive trade and bring price recovery.

When the depression actually commenced, the business community suggested either direct help to trade and industry or artificial check to foreign imports. They demanded a substantial reduction of railway freight on agricultural products, the imposition of import duty on wheat and rice, a revision of land revenue policy so as to afford adequate relief to agriculturists, and measures for facilitating marketing, warehousing, financing and movement of crops. On the whole, the business community suggested a policy of economic nationalism, although it must be mentioned that the devaluation of the rupee always remained a plank in their contention. Some of these suggestions were later on revived, only with a difference of outlook. While subsidy and State help were at first advocated from a spirit of economic self-sufficiency at any cost, they were later on favoured in order to put purchasing power in the hands of the people or as a part of a wider economic planning.

By 1931 and 1932, when the price depression was at its bottom, economists of the West were propounding a new analysis of the situation and suggesting new remedies. Indians at once fell in line with the new contribution to economic thought. They were singing to the tune of economic planning and economic control. With the advantage of cheap money, a large-scale loan expenditure was suggested in order to put purchasing power in the hands of the people. By 1934 catchwords like economic planning or reflation were very much in the air. At the same time, Indians were witnessing in the West an application of economic nationalism through tariffs, bilateral trade agreements, control of imports and exports, restriction of production, and mutual marketing arrangements. The business community in India got encouraged. They suggested similar policies for India with fresh ardour. Along with these

demands there was an advocacy of debt conciliation. This idea was also a foreign import, the model having been derived from Roumania in 1931. Most of these remedial measures were suggested by the business community which looked upon them as highly efficacious for industrial and trade revival. All rational economic thinkers, on the other hand, considered them short-sighted, and as likely to aggravate the depression. But economic planning, cheap money policy, public works expenditure secured the support of able economists.

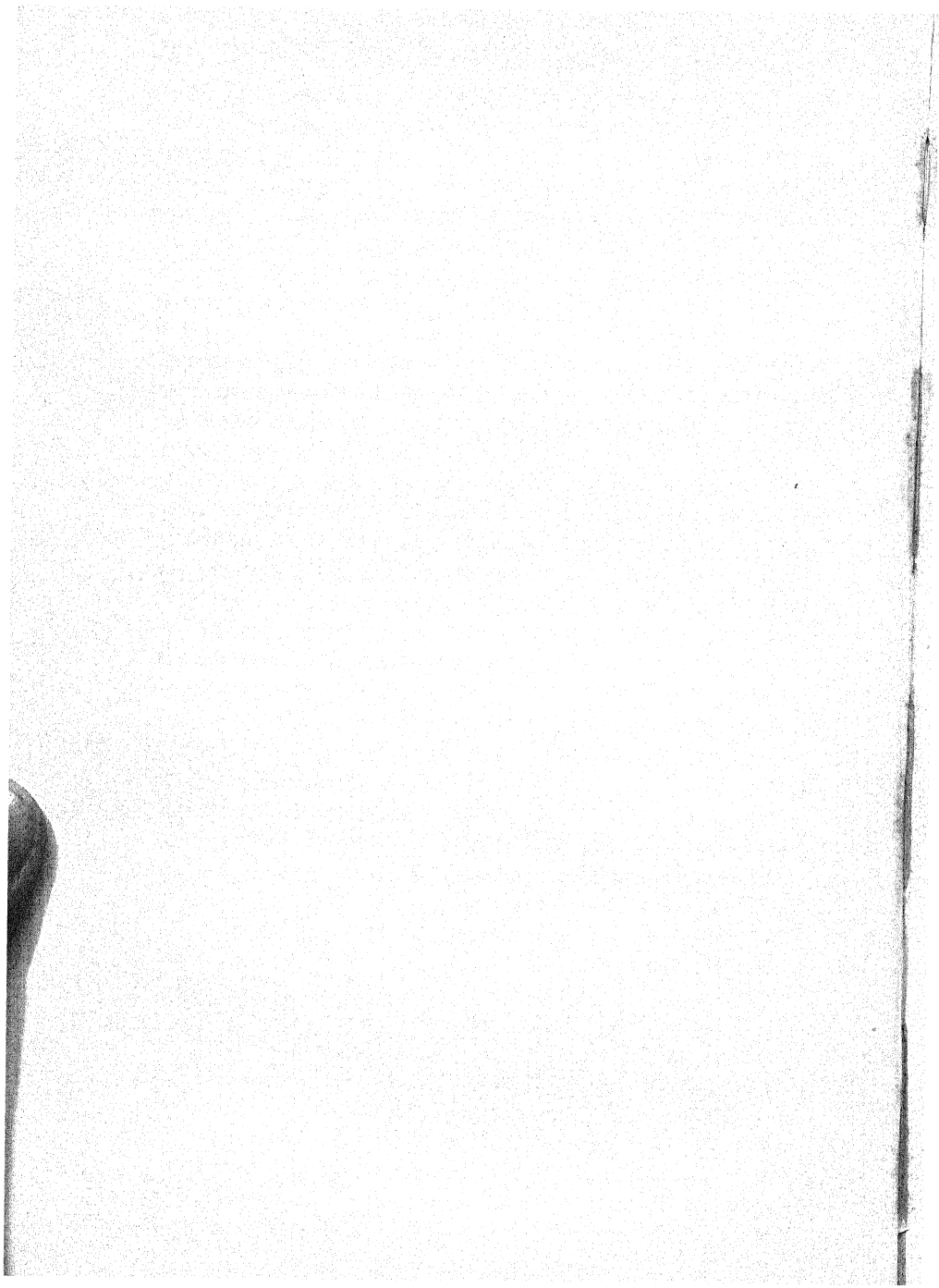
On the analysis of the causes of price depression there was not always that unanimity of opinion. Nor were the Government of India by tradition and outlook in a position to accept the means suggested. On currency and tariff policy, the difference of opinion among the people was wide enough, while the Government of India were definitely in favour of the policy they adopted. The idea of economic planning had a large number of advocates in the country. No one, however, approached the problem with a practical outlook. In a vast unorganised society where individuals do not realise the necessity for social allegiance, controlled regulation of economic destiny was impossible. The political status of the country is not such as would allow the Viceroy or any Governor to adopt whatever policy he would like. Some of the suggestions for recovery were adopted piecemeal. Tariff duties on certain imports were maintained and sometimes enhanced; crop restriction schemes were experimented with here and there; and debt conciliation schemes were brought into existence in certain Provinces.

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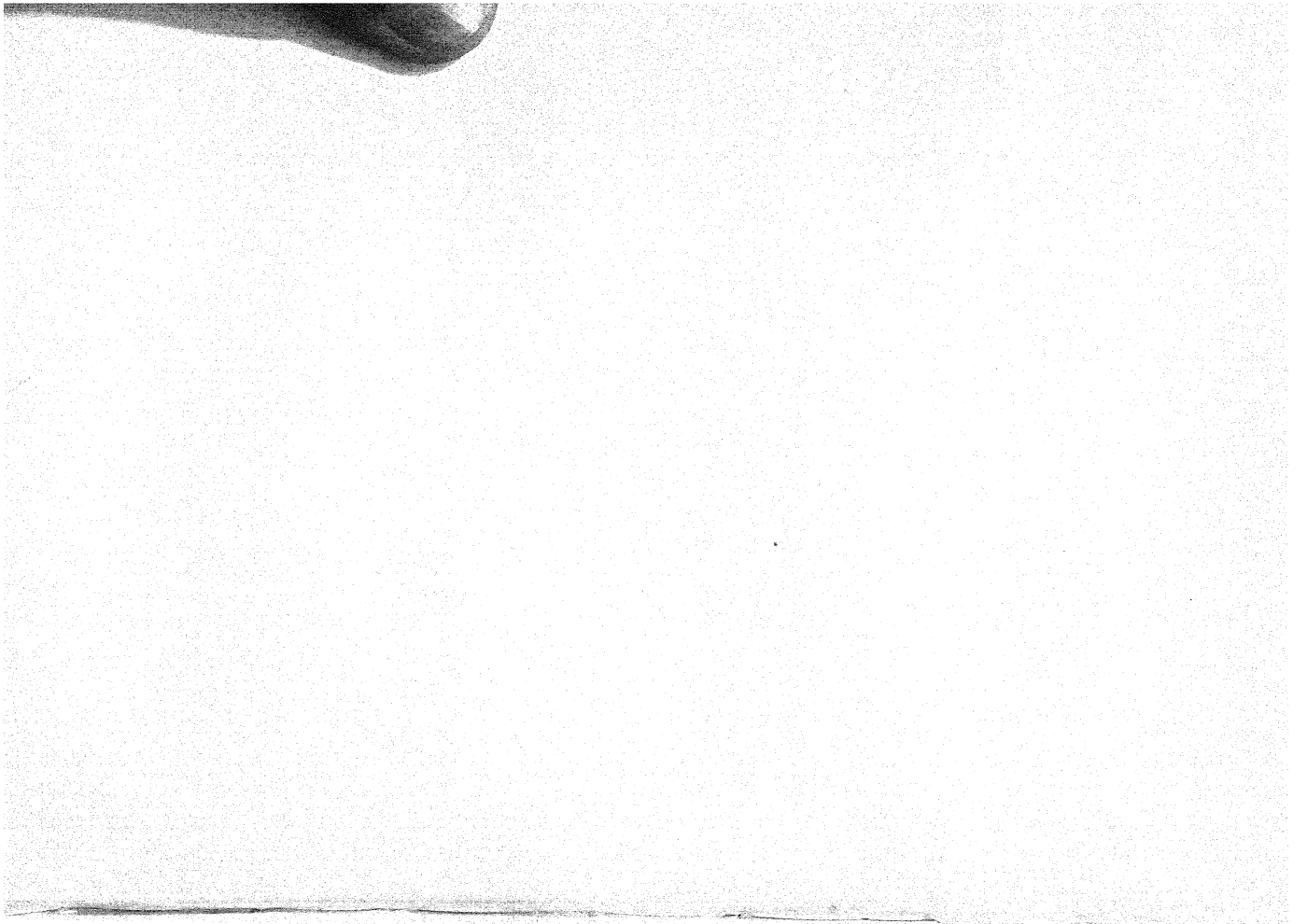
Conclusion.—The problem of India is peculiar to her. As the articles of production generally consist of foodstuffs and raw materials, their demand is often inelastic. If for any reason there is price depression, restoration becomes extremely slow. It does not become automatic. Depression becomes tenacious. Food articles, for example, decline in

price not so much due to contraction of desire as for other reasons. It is for want of purchasing power. Price recovery of raw materials is, however, very much dependent upon industries. The effect of industrial recovery upon them is usually late in coming. This is one of the reasons why price revival in India is sluggish, although recovery is in evidence in other countries.

At present what India requires is to give greater attention to the increase of the efficiency of production and marketing rather than attempt to raise the price level by artificial means. A portion of the lost market of the world should be at least regained and the demand for Indian commodities increased. At the same time India should try to intensify the demand for her raw materials and primary products by organising new industries within her national borders and discovering new industrial uses for these commodities. The new industries will be new sources of employment of middle class people as well as of those who cannot otherwise adopt agriculture. Their employment will greatly increase the demand for all commodities of Indian origin and national and local balance of payments will be restored. There will then ensue national recovery and national welfare.



Part VI
PUBLIC FINANCE



CHAPTER XXXII

FEDERAL AND PROVINCIAL FINANCE

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Changes in the Financial Perspective.—It has been well said that finance is a handmaiden to politics in the widest sense of the term, and it is no wonder that recent changes in the political constitution of the country should have awakened a fresh interest in the subject of Indian Public Finance. The liberalising of the Provincial constitutions and the introduction of an element of popular responsibility in the Central Government of the country are bound to alter, if not financial analysis, at any rate, financial perspective. The impending establishment of a Federal Government for the whole country is also an event which is calculated to modify many aspects of Indian finance. It has become necessary to take stock of all these changes in our interpretation of the Indian financial problem.

Dependent Government.—Till the year 1921, when the first beginnings of responsible government were made in the Provinces, the finance of all Governments in India was a matter wholly dependent on the wishes of the Secretary of State for India and his agents in this country. The fact that the political control of Indian policy vested in the members of the British Cabinet had an undeniable and far-reaching effect on the working of the Indian financial system. The case of Indian tariff policy is well-known. In opposition to the combined wishes of the Government and people of India a free trade, and later on a low tariff, policy was imposed by the Secretary of State who was primarily influenced in this connection by the representations received from the Lancashire cotton industry. On the side of expenditure such items as the

composition, equipment, salary and employment of the Army in India were decided with reference to Imperial defence policy, which was entirely outside the influence of Indian authorities. That both the revenues and expenses of India were powerfully affected by these external influences is undoubted.

Since the year 1921 a slight change has taken place in this abnormal, and in the strict sense unnatural, situation. Both in the Provinces and in the Centre legislatures have been set up with preponderant elected majorities. In the Provinces the official bloc has been removed altogether. Under the Act of 1919 no alteration in the tax system could be effected without the concurrence of the Legislatures, though both the Governors and the Governor-General had powers of certification by which tax measures could be enacted by them in opposition to the will of the Legislatures. As for expenditure a considerable field was beyond the control of the Legislatures, as the demands for grants falling in that sphere were not submitted to vote. The right of restoration of grants vested in the Governors and the Governor-General robbed the Legislatures of any real control over the expenditure side almost as surely as in the case of taxation. Under the Montague-Chelmsford Act, from 1921 to 1937, the right of restoration of grants and certification of taxes was freely used by the Governor-General, though it must be admitted that its use was very rare indeed in the Provinces.

Under the new constitution which has been initiated in the Provinces since April, 1937, the direct control of the executive heads over both taxation and expenditure has been considerably reduced. The special responsibilities of the Provincial Governors and the Governor-General, and the reserved departments under the control of the latter, are items of expenditure for which the ultimate control vests in the highest executives as before. But the power of certification of individual tax measures is removed and the executive has no more than a first charge over the revenues for special and essential expenditure. The Governor-General possesses, moreover, a special responsibility under the Act

for the financial credit and solvency of India. His general control over financial and borrowing policies is an important limitation on the fiscal freedom of both the Central and Provincial Legislatures.

Provincial Autonomy.—It must none the less be admitted that the sphere of influence of the Provincial Legislatures over Provincial finance has considerably increased. The important limitations that still operate are more on the side of expenditure than on that of revenue. The most glaring case is that of the recruitment and salaries of what are called the security services. These are entirely under the control of the Secretary of State. In the centre all the defence services, in addition to the Civil and Police services, are thus excluded from popular control. Taken together all these items of expenditure stand for a very large portion of total governmental expenditure and the judgment of the representatives of the people can in no way affect either the principle or the extent of the resulting burden. That the present organisation of superior services is too elaborate and too costly is an opinion universally held in India, though it is stoutly resisted by English official opinion. The Indianisation, cheapening and simplification of administrative organisation are matters in respect of which the political interests of the British Government in India are the principal consideration at present. In so far as these items now stand for a higher figure of expenditure than what would be spent on them if the final control over them were to be transferred to popular Legislatures, they must be considered as accompaniments of a subordinate political status, and allowed for as such in any scheme of financial reform.

That finance can hardly ever be dissociated from political jurisdictions is a matter that will become increasingly apparent as the federal character of the new Indian constitution unfolds itself. It is interesting to note in this connection that the beginnings of administrative decentralisation in British India, out of which the idea of a federation had, later on, its birth, were originally made on account of financial considerations. The wastefulness of expenditure in the Provinces and the unproductiveness of their tax

collection led to a realisation of the superior virtues of local autonomy and responsibility. From the financial to the administrative and from the administrative to the political spheres, this principle of local autonomy has continued to grow, so that it has now been translated into the governing principle of the Indian constitution. Except the Indian States, who will come into the all-India federation by a process of accession, the rest of the governmental authorities in India must be said to be the products of the process of financial and administrative decentralisation.

With decentralisation of functions naturally goes the extension of popular control over local expenditure. In a federal constitution there are three distinct stages of governmental authority, namely the national, the provincial and the municipal or local. Though the extent of autonomy and the magnitude of functions allotted to municipal and local authorities compare poorly with the imposing and semi-sovereign status of the Provincial Governments the primary need of having a satisfactory financial system to subserve the administrative ends is as great in local as in provincial and national Governments. Public expenditure at all these stages of administrative organisation must ultimately come out of the total national dividend, the nation's purse. Unless the people as a whole control all these stages of revenue and expenditure it cannot be said that the best possible utilisation of the nation's public resources has been brought about. The incomplete control exercised by the electorate on the national finances is bound to circumscribe the extent of its control over provincial and local finance as well. Not till the entire field of revenue and expenditure in all the stages of government has been placed under popular control can it be said that Indian finance has attained a normal constitutional position.

But the business of government must go on in the present semi-responsible constitution. In fact the success of responsible government will depend upon and will be measured primarily by its achievements in the financial field. How far the alleged evils of unequal and burdensome taxation on the one side and of wasteful and unproductive

expenditure on the other can be removed by the new Governments in the Provinces is a matter for speculation. It is, however, clear that all the new Governments have to work out their administrative and financial programmes under very serious limitations on their freedom of action. Circumscribed as their opportunities are, they will find immense advantage in a systematic study of our entire fiscal system. In one sense the study of Indian finance was never so realistic as it is at present and all authorities on whom lies the responsibility of decision will do well to find out the methods by which they can at once remove the blemishes of the tax system and use it for furtherance of the wider objects of social amelioration and national reform.

Federal and Provincial Finance.—As the Indian constitution is essentially a federal constitution the spheres of financial action of the Federal and the Provincial Governments have necessarily to be defined in a more or less explicit manner. The source of Indian federalism is nowhere more in evidence than it is in this respect. When the process of decentralisation commenced the Provinces hung upon the concessions made to them by an all-powerful central and, in a sense, paternal Government. The independent identity of Provinces as fiscal and administrative units was not recognised as a principle, and in all matters of doubt the Central Government's needs, as it chose to define them, had the last word. Neither the Provincial Governments nor the citizen body as a whole had any co-ordinating and decisive control in the matter. Indian economy being a backward and very slowly moving system of production, the utmost importance attaches to the items and the level of expenditure. As the Central Government has at least two departments of expenditure which between themselves answer for over one-third of the total public expenditure in India, the policy underlying these items, namely defence and superior civil services, inevitably conditions the success of all reforms in the direction of introducing schemes of genuine federal finance.

If the Government of India must have, for reasons over which the representatives of the people have no control, about 50 crores of rupees for their defence budget and about 10 crores for payment of the superior civil services whom they employ, the extent to which they can part with sources of revenue in favour of the Provincial Governments is strictly limited. It has now been admitted on all hands that so far as the merits of the case go, the Provinces must be admitted to a considerable share of the income tax at present raised and, for the most part, appropriated by the Central Government. The claims of justice in the distribution of central burdens and of adequacy in the provincial revenues cannot be even remotely satisfied unless the most important direct tax on non-agricultural incomes is adequately shared by the Provinces. The Government of India Act provides for a progressive sharing of a prescribed portion of the proceeds of the personal income tax with the Provinces. But the working out of this scheme of sharing is made to depend upon the discretion of the Governor-General, who will satisfy himself that the soundness of the central finances is not adversely affected by such sharing. The expenditure of the Central Government, contrary to the expectations of financial experts like Sir Walter Layton, has proved inelastic. In fact, owing to the new urge for the improvement and augmentation of armaments, as also to the increased demands on the co-ordinating and supplementing activities of the Central Government, its expenditure is more likely to increase than to decrease. When the Federation comes on the scene the administrative charges of the Central Government will also mount up.

Under the circumstances any large scale sharing of the proceeds of the income tax depends primarily on the probable yield of the other sources of central revenues. The customs tariff is at present fairly high and with the progress of the policy of protection the utmost that can for the present be expected from this source is that it will not shrink. The finance member of the Government of India has often warned the enthusiastic protectionists of the adverse effect that their policy is bound to have on the yield of the customs revenue.

Whatever might be the practical implications of such a caution, the customs revenue can hardly be expected to increase to such an extent as to create a surplus in the central budget, so that the sharing of the income tax might be hastened. It must, moreover, be remembered that the present rates of customs duty are more or less at an emergency level and their scaling down rather than their augmentation is the legitimate objective towards which central financial policy ought to aim. Of the other sources of central revenue, unless the prevailing opinion on the subject changes radically, neither opium nor salt may be expected to bring an increased amount into the central exchequer.

Railway Contribution.—We are thus left with the railways as the probable saviour of the desperate financial situation created for both the Central and the Provincial Governments. By the creation of a separate statutory authority for the railways the direct control of the Indian Legislature over their finances and administration is now ruled out. Even if we agree to look upon the railways as primarily a public service such a complete separation of their finance from the general financial organisation can hardly be justified. When all is said and done, the railways are a public monopoly in India, and whether we call their collections rates or taxes, a very important share of their proceeds partakes of the characteristics of taxation. The total gross revenue of the Indian railways is in the neighbourhood of 90 crores of rupees, fully equal to the yield of all other central levies. If the control of the Central Legislature over the taxation of the people is to be complete, railways no less than the other sources of direct and indirect revenue, ought to be amenable to the normal financial procedure. Whether it is in principle a sound system that the railways should contribute to public revenues is not an open question in India. For reasons which are writ large in the history of the Indian railways, a small percentage on the total capital at charge with appropriate deductions is held to be an integral part of the central revenues. The reopening of this question at a critical stage of our financial and political evolution will spell nothing but financial chaos and disaster. Any definite

programme of federal and provincial finance can now proceed only on the assumption that the liability of the railways to contribute the fixed quota of 1 per cent remains intact.

If a stable system of federal finance is to be established in India we must all make up our minds about a preliminary issue. The doctrine of a clear-cut separation of functions and resources as between the Central and the Provincial Governments on which the Montague Report laid such great stress is impossible of practical application. In the peculiar mood of the times, when the provincial administrations were apprehensive of a continuation of central interference, there was some justification for enunciating such an absolute rule, though even then it could not be applied in practice and the provincial contributions had to be provided for. The new constitution by its procedure of treating all governmental authority in India as first surrendered to the Crown and then redistributed as between the Central and Provincial Governments has removed all the causes of a justifiable apprehension on the part of the Provincial Governments. The subject of financial relations between the Federal and Provincial Governments can now be approached from a purely objective standpoint.

Financial Co-operation.—In all federations there is a definite tendency towards a growing integration of economic organisation. Most of the processes of production and exchange, especially those which are conducted on a large scale and on organised lines, have a tendency to spread over the country without any reference to the different local administrations. The regulation and taxation of these activities clearly falls within the competence of the national Government. As, however, this legislative and fiscal activity creates no corresponding charge on the disbursing side of the Central Government, and as in fact the Provincial Governments have to provide for many costly administrative services for such activities, the proceeds of such national taxation must necessarily be shared with and distributed among the Provinces. Many a source of taxation, moreover, such as succession duty, is inevitably bound up with the general civil and procedural

law of the country. In the interest of uniformity of treatment and appropriateness of procedure several items of revenue have thus to be centrally treated.

Nor can the needs of central expenditure on subjects which primarily fall within the sphere of Provincial Governments be altogether ignored. With a view to ensure a minimum standard of efficiency in respect of important departments of State activity, especially those which aim at social and economic betterment, the Central Government has to assume a definite responsibility which it cannot abandon even in a federation. Even apart from the needs of uniformity, the function of leadership, guidance and co-ordination in an increasing number of public activities almost automatically falls on the shoulders of the Central Government. Irrigational and industrial research, hygienic and medical investigations, not to mention the ever-increasing activity of the central agricultural organisations, clearly stand for a category of functions which are bound in future to make an increasing demand on the resources of the Central Government. Any preconceived notions about mutual exclusiveness of central and provincial items of revenue and expenditure, and especially of the stationary or dwindling items of expenditure in the national Government, appear, therefore, to be unfounded. We must proceed along the path of financial co-operation between the Federal and the Provincial Governments.

That such a course is inevitable is seen from experience of most federations, and even the short experience in India tends to prove the same thesis. It is, however, felt by some students of the subject that if the Central and the Provincial Governments thus come to have an interlocking of their financial organisation the limits of their administrative control and political responsibility are likely to get blurred. That there is some foundation for these fears must be admitted. Federation, and in fact all government, is, however, a matter of compromise between divergent social tendencies. The contrast between economic integration and political differentiation that inevitably develops in a federation cannot be resolved except through the process of a

sharing of common revenues and of inviting the Central Government to play an important role in several departments whose administration is primarily left to the Provinces. The development of an institution such as an Inter-provincial Council, representing the finance departments of the several Provincial Governments, might give to the constituent Provinces a well-marked share in controlling the raising and disbursement of common funds. The Governor-General in giving his prior consent to measures of taxation coming before the Central Legislature, in which the Provinces are interested, and generally in respect of matters affecting the finances of the Provinces, should as a rule be required to consult the Inter-provincial Financial Council. The chief co-ordinating and reconciling factor will, however, remain in the common sovereignty of the electorate both over the Federal and the Provincial Governments.

Central Guidance.—Wherever definite sources of revenue or a common provincial fund is to be shared among the Provinces an interprovincial administration of these sources and funds under the auspices of the Federal Government can be easily worked. Wherever an interlocking of resources or expenditure appears to be necessary as between the Central and the Provincial Governments a common administrative organisation should be set up. This course will be in keeping with the political tenets of federalism, wherein the autonomy of the parts is at least as important as the co-ordinating authority of the centre. But in certain cases the Central Government feels called upon to make earmarked grants or subventions to the member Governments. In this case the recipient Governments have no control over the policy underlying the grants and their dependence for any but the comparatively unimportant parts of their activity on such a source would be financially and politically unsound. In several cases these grants are deliberately used by the Central Government to influence the policy of Provincial Governments in primarily provincial matters in a way which the national Government approves. Here the grants are used not primarily as a method of supplementing provincial resources but as an instrument of administrative regulation

of provincial policies at the hands of the Central Government.

In a continental federation, such as India is likely to be, and especially with the hesitant Indian States thrown in, a plausible case can indeed be made out for the use of the financial arm of the Federal Government to secure a certain minimum degree of co-ordination and efficiency in important matters of public welfare. The traditions of centralised rule in India are, however, at least as pronounced as those of provincial separatism. For the immediate future at any rate the extension of the practice of federal grants must be discouraged as it materially hampers the freedom of provincial action and weakens the sense of responsibility. Thus the grants for rural reconstruction far from putting the Provincial Governments on their mettle to cope with an important object of State activity only tended to weaken the sense of their own responsibility in the matter and taught them to look to the Central Government for guidance in an essentially local matter. Apart from the merits of the case the use of the grants out of the Road Fund to influence the road construction policy of the Provincial Governments so as to subserve the ends of the Central Government's railway policy, over which the Provinces have no control, must also be looked upon as a bad beginning. If grants are inevitable their administration should be, at any rate for the immediate future, under the control of the representatives of the Provincial Governments along with those of the Central Government.

Present distribution of resources.—The need for additional revenues for the Provincial Governments is, however, so great that they are learning to be grateful for small mercies without reference to the theoretical merits of the underlying principles. The dissatisfaction felt by all sections of expert and lay public opinion in India with the present organisation and payment of the military and civil services has already been mentioned. The adoption of a policy of reduction and eventual abolition of British troops in India, the Indianisation of the ranks of officers in all the branches of the defence

services, and the increased Indianisation and cheapening of the civil services are reforms which are overdue and are calculated to create a saving of at least 10 crores of rupees in the central budget. The hostile reception meted out to these proposals by British authorities is primarily based upon political considerations which a large mass of responsible Indian opinion does not share. Can we for this reason refuse to face the immediate problem of federal finance in India and make its solution contingent upon the dawn of full responsibility? Such a course may appeal to some people, but a little consideration will show the futility of this attitude of negation. Events in this sphere are more powerful than men and it is the part of practical statesmanship and financial wisdom to try and regulate the events as far as possible in conformity with the accepted canons of reform.

Provincial Dissatisfaction.—Many a Provincial Government, including the respective Governors, have publicly declared their dissatisfaction with the existing distribution of resources between the Central and the Provincial Governments, and have even openly worked for its modification. In the past, that is before 1921, an arbitrary standard of expenditure was fixed for each Province, without any systematic attempt at equality of any sort. As the scheme of provincial contributions known as the Meston Award was primarily based upon this level of expenditure in the various Provinces injustice done in the past to certain Provinces, who paid to the central treasury a larger share than certain other Provinces but in return got a much lower amount to spend, was in a sense perpetuated. But the same scheme of distribution initiated another glaring inequality between Provinces with developed industries and those with comparatively undeveloped industries. While the Provincial Governments had to incur an increasing expenditure for their entire population, agricultural and non-agricultural, they could in effect tax only the agricultural section, the non-agricultural sections being taxed by the Central Government. This was hard on all Provinces, but especially injurious to those who have a large portion of their population employed in non-agricultural pursuits.

The abolition of the provincial contributions removed the older grievance but left the new one intact. Overshadowing and in fact accentuating this evil of inequality is the great problem of paucity of provincial resources. If the Provincial Governments of the future are to promote the welfare of the people they must either economise, or tax, or do both. They can hardly wait for the large economies which can only take place when the process of the establishment of responsible government is complete. They have to conduct the administration in an efficient and progressive manner from day to day. They must, therefore, take account of their existing resources, and while working for the early fruition of the large-scale reforms that can come only after the establishment of full responsibility, they must seek out ways and means to finance their immediate programmes.

The Niemeyer Award.—In this empirical sense the recommendations made by Sir Otto Niemeyer appear to be the nearest approach to a solution of the problem that can be secured for several years. Sir Otto took for granted the present scale of expenditure in the Central Government and felt that unless the railways began to pay their prescribed contribution to the general revenues a sharing of the personal income tax with the Provinces was not a feasible proposition. How theory and practice often loudly conflict in public finance is best illustrated by the changing course of authoritative recommendations regarding the sharing of the Income Tax in India. The Federal Finance Sub-committee of the First Round-Table Conference (Peel Committee, 1931) accepted the general principle of the provincial claim to a share in the proceeds of the Income Tax. The Federal Finance Committee of 1932 (the Percy Committee) was so much impressed by the arguments in favour of the provinces' claim to income tax, that they recommended a virtual surrender of all the proceeds of personal income tax to the Provinces, sanctioning, if necessary, the reintroduction of provincial contributions to the central exchequer. Theoretically this was the soundest course to follow, but the Provinces would not hear of any reintroduction of contri-

butions, nor was the Central Government eager to renew its dependence on provincial subsidies.

The White Paper on Indian constitutional reforms, therefore, provided for a sharing of the proceeds of the personal income tax collected in the Provinces. The minimum share of the Provinces was to be half and the maximum three-quarters. Both the Central and Provincial Governments were to be free to levy a surcharge of their own, provided the provincial surcharge did not exceed 12½ per cent of the main demand. Even this recommendation, however, could not be eventually adopted owing primarily to the growing financial stringency in the Central Government. The needs of rearmament and of subsidies to deficit Provinces on the one hand, and the dwindling yield of the railways on the other, made an immediate or an early sharing of the income tax an impossible proposition. The Government of India Act, 1935, left the commencement of the period and the proportion of provincial sharing in the income tax to be determined by an Order-in-Council. No minimum percentage was prescribed and an initial period of some length over which the Provinces would not get any share, or would get less than the full prescribed share, was allowed. Even after the commencement of the scheme of a progressive sharing of the income tax with the Provinces the Governor-General is given the discretionary authority to suspend, for reasons of stability of central finances, the operation of the scheme for any length of time.

Examination of the Niemeyer Award.—Sir Otto Niemeyer was specifically charged with the responsibility of declaring whether the financial condition of the Central and the Provincial Governments would be sufficiently strong to make the inauguration of the new constitution a safe proposition. It was quite natural that Sir Otto should pay more heed to the necessity of placing the tottering provinces on their legs and of ensuring the continued financial strength of the Central Government, than to meting out strict justice to all parties. By recommending the wiping out of certain outstanding debts of the

Provinces to the Central Government and by enhancing the initial and annual subventions to Provinces in a few cases, Sir Otto secured the solvency of the autonomous Provinces, at any rate during their early years of the working of the new constitution. Such questions as the probable return on the large amounts sunk in the Sukker Barrage, or the likely needs of a Province like the Frontier Province are hardly capable of being finally settled in advance. By recommending that for the first five years of the federation no amounts out of the yield of income tax collected in Provinces be shared with them, and that even thereafter the scheme of sharing by five equal stages be initiated only if the total sum of the provincial share of the income tax, *i.e.*, half of the income tax collected in the Provinces on other than federal incomes, and the railway contribution to the general revenues reached the figure of 13 crores, Sir Otto also secured the continued solvency of the central budget. He had to recommend, taking into account the increased strain on the central resources caused by the proposed enhancements of subventions and the gloomy prospect of the railways, that the additions to the income tax and some of the other taxes made during the period of emergency created by the depression should not be removed, at any rate till the financial position of the Central Government considerably improved.

Sir Otto Niemeyer's recommendations had clearly been based on grounds of expediency and compromise rather than on grounds of theoretical accuracy or fiscal justice. For instance there is reason to believe that he did not see the validity of the claims of the jute-producing Provinces to a prescribed share in the proceeds of the export duty on that article. As, however, half the proceeds of that duty were already surrendered to the Provinces concerned he recommended a further sharing of $12\frac{1}{2}$ per cent. With regard to the basis of distribution of the provinces' share of the income tax Sir Otto showed himself to be equally keen to arrive at a definite standard based on rough justice. Neither the population of a Province nor the residence of the tax-payer can be said to possess any dependable relevance to the underlying claim, though both these criteria

were pressed upon his attention by Provinces concerned. As will be seen from the table on the page opposite, Sir Otto by combining both these bases and by allowing for other factors peculiar to each Province arrived at a standard schedule of proportions, which was on the whole a satisfactory solution of a very difficult problem.

In a sense, however, the solution of the problem of federal finance recommended by Sir Otto Niemeyer is no solution at all. He recommends in effect the prolongation, if not perpetuation, of the *status quo*. Well might some of the Provincial Governments say, "while the grass grows the steed starves." The maximum share that the Provinces can ever hope to get out of the income tax is now fixed as a percentage of half of the net income tax collected in all the Provinces from non-federal incomes, though at one time it appeared that the maximum amount to be distributed among the Provinces would be a higher fraction than one-half. Moreover, as the sharing of the income tax is made contingent upon the improving yield of the railways, the Provinces are thrown at the mercy either of the improvement of traffic or the reorganising zeal of the railway authority.

The improvement of traffic is a very problematical and at best a very slow process. There is a definite augmentation of economic activity, thanks partly to the upward curve of the business cycle and partly to the rearming activity of most countries. It might, therefore, be expected that the traffic returns of Indian railways will show an improvement in the near future. The volume of this improvement is, however, a matter for speculation. Whether in the near future it will be so striking as to increase the net yield of the railways, say, by 6 or 7 crores is, to put it mildly, very doubtful. How much of the enhanced traffic will be carried by road, and how far the railways will continue to suffer from competitive modes of transport, are important but uncertain factors in the situation. The attempts now contemplated by the Government of India to restrict road transport, though based on a good principle, are lacking in comprehensiveness. Unless the cheaper and more convenient means of trans-

Province 1	*Population, 1931 census* 2 (*lakhs*)	*Percentage of total* 3	*Income tax collected in the Province* 4 (*thousand rupees*)	*Percentage of total* 5	*Half of columns 3 and 5*	*Percentage of total distributable income tax recommended by Sir Otto Niemeyer for the Province* 6
1. Bombay	230	8·5	43,758	33·3	20·9	20 Bombay 2 Sind
2. Madras	472	17·4	17,759	13·5	15·4	15
3. Bengal	511	18·8	35,981	27·4	23·1	20
4. United Provinces	496	18·3	11,772	9·0	13·7	15
5. Punjab	280	10·3	9,192	7·0	8·7	8
6. Bihar and Orissa	423	15·6	6,110	4·6	10·1	10 Bihar 2 Orissa
7. C.P. and Berar	155	6·0	3,399	2·6	4·3	5
8. N.W.F. Province	47	1·7	1,128	1·0	1·3	1
9. Assam	92	3·4	2,136	1·6	2·5	2
Total	2,706	100·0	131,235	100·0	100·0	100·0

port, namely the bus, is recognised as an integral part of our transport system no satisfactory solution of the problem of the so-called road-rail competition can be found.

Rail-Road Co-ordination.—This is essentially a problem in which the interests of both the Federal and the Provincial Governments are involved. Unless the Provinces are well assured that a fair deal is being meted out to the road transport in which they are primarily interested, they will not be willing co-operators in a policy of bus regulation. To carry such an assurance to the Provinces not only must the measure of regulation be so devised as to provide for normal expansion of road traffic, but the special claims of the railways must also be fully justified. There is a feeling among many responsible sections of public opinion that the Government of India are unwilling or unable to remove the more serious causes of railway deficits, and are using their position as the supreme Government and as the disbursers of the road development fund to shelter the inefficient railway lines from fair bus competition. Such feelings may conceivably be based on incorrect notions. But so long as the evidence supplied by heavy motor taxation has not been counteracted by a detailed investigation into the organisation and prospects of the bus industry there is every danger of the Central Government's insistence on road traffic regulation being attributed to its partiality for its own interest in the railways.

As regards the railways themselves the experts' committee led by Sir Ralph Wedgewood has come out with a very disappointing report. In certain respects, such as the costs of working and organisation, the committee has not been as thorough and independent in its inquiry as it ought to have been. Like some other expert committees visiting India for a short period and reporting on important matters of national economy, they seem to have been led by the departmental views supplied to them. On the other hand they have expressed opinions on subjects which either were not referred to them or were not really within their normal competence. That the railways should not be called upon to make any contribution to the general revenues and that the prospects before the railways are none too hopeful are

observations which have no relevance at all to the main task set to the committee, that of recommending a more economical organisation for the railways. An historical as well as theoretical grounds the railways in India have to be considered an important contributory to the general revenues. Fortunately, there is reason to believe that the actual experience of the railways in the near future will be more hopeful than the committee contemplated.

An improvement in traffic accompanied by a well thought out measure of co-ordination between rail and bus traffic will bring about an early increase in the net earnings of the railways. In the meanwhile the yield of the income tax will also increase on account of improving business conditions. Though it is very difficult to forecast such things, it can even be said that unless an unforeseen check is placed on the normal process of the improvement of business and of public revenue the scheme of sharing suggested by Sir Otto Niemeyer can come into operation even earlier than five years after the establishment of the federation. It must, however, be admitted that there is a considerable element of uncertainty both in the economic and administrative factors involved, and the Provinces can hardly base their budgets for a long time to come on an anticipated receipt of their full share of the income tax. Far more important than the date of distribution is the size of the provincial share of the income tax. On the basis of 6 crores as the total distributable share of the income tax the several Provinces will get the following amounts under the schedule recommended by Sir Otto Niemeyer :—

Province	*Lakhs of Rs.*
Bombay	120
Madras	90
Bengal	120
U.P.	90
C.P. Berar	30
Assam	12
Sind	18
Punjab	42
Bihar	60
Orissa	12
N.W.F.	6
Total	600

Provincial Needs.—Considering the pressing exigencies of provincial finance it can hardly be said that the relief to be obtained by the proposed distribution of half the proceeds of the income tax is likely to be either timely or adequate. It is, however, possible to belittle the significance of the accession to the provincial revenues that the receipt of a share in the income tax would mean. Thus in the case of Bombay the first ministry under the new constitution had produced a programme of reforms which would have put the provincial revenues to the net expense of exactly the same amount which the Province expects to receive when it gets its full share out of the distributable sum of income tax. An early sharing of the full proportions recommended by Sir Otto Niemeyer is, therefore, a very desirable step, and even at the cost of continuing some of the exceptional measures of emergency taxation the working out of the Niemeyer award should be expedited. An improvement in economic conditions coupled with a wise yet firm handling of the rail-road issue ought to make this possible.

Such a course would no doubt facilitate the immediate task of Provincial Governments. The most pressing reforms in the direction of remission of taxation, especially of the land tax, and of improving the educational and health services can be financed out of added resources which the Provincial Governments would receive when a better distribution of the existing resources between them and the Central Government is brought about. But for their further progress the Provincial Governments would need an expanding revenue, and this they will have to secure mostly from their own resources. In view of the financial situation at the centre any further sharing in the federally collected excises, than at present, is not a very hopeful prospect. The difficulties in the way of getting the Central Government to levy a succession duty on non-agricultural property or on the movement of goods and passengers with a view to distribute the proceeds among the several Provinces are too great to be removed in a short time. The ideas underlying these measures will have to be popularised for a long while before they are formally proposed. The machinery

of tax administration will also have to be steadily improved. The same considerations apply to the introduction of a succession duty on agricultural property in the Provinces, though it is easier from the administrative standpoint to introduce this measure than the wider one. In any case legislation at the hands of the Central Goverment, in some shape or another, would appear to be inevitable, and as a ready remedy for improving their financial position the Provincial Governments can hardly depend upon the powers conferred upon them to tax succession to agricultural property.

Fresh Taxation.—A more elastic and sympathetic land revenue policy, a more determined progress towards prohibition, a large scale improvement in the beneficent services, above all a measure of redistribution of wealth in favour of the poorer sections of the population—these and many other similar reforms that are being enthusiastically canvassed among the new legislators can hardly be financed without a fresh measure of taxation. The inability of the Central Government to part with a share of the income tax at an early date is likely to lead the Provincial governments to take an earlier resort to fresh taxation. In any case fresh taxation would be inevitable, and the least objectionable method of resorting to it is to proceed to tax those classes of non-agricultural incomes which at present either pay no direct tax, or pay it to the Government of India which is unable to share it at an early date with the Provinces. This can be achieved by instituting a system of professional and turnover taxes which are within the full competence of the Provincial Governments. These taxes dropped during the British régime are by no means unfamiliar to Indians. Under a different name they obtained under indigenous Governments, and as a supplement to land revenue on the one hand and to income tax and super tax on the other their use would appear to be particularly appropriate in a country of small professional incomes such as India is.

The level of present administrative expenditure in the Central as well as the Provincial Governments is to an important extent determined by authorities other than those responsible to the Indian legislatures. There is reason to

believe that considerable saving can be effected by the process of Indianisation and reorganisation, neither of which can be undertaken in our present constitutional position. The unpopularity which is inseparable from all fresh taxation is likely to be heightened in the present case by the knowledge that the imperfect realisation of responsibility is an important cause of the added burden. If, however, fresh burdens fall on those who are at present being treated, though not deliberately, in a preferential way the grounds for dissatisfaction will be considerably reduced.

The position created by the paucity of important sources of revenue and the demand of more than one Government to exploit them in its own interest leads either to a sharing of the commonly collected tax, as is proposed in the case of the Indian income tax, or to the system of surcharges. The White Paper on Indian Constitutional reforms provided for a scheme of double surcharges on the income tax. A basic rate was to be levied by the Central Government, and it was to be open to both the Central and Provincial Governments to levy further surcharges, under certain restrictions, in their own particular interest. This course was, however, found to be unsuitable in view of the needs of inter-provincial uniformity, and hence while it is not now allowable for a Provincial Government to levy any surcharge, the Central Government is free to levy a special surcharge not only on the income tax, but also on those sources of revenue which the Central Government is to levy with a view to their distribution among the Provinces, such as succession duty on non-agricultural property and terminal taxes. In spite of the undoubted theoretical objections to local surcharges on the income tax, their retention in the armoury of the Provincial Governments, subject to suitable safeguards as in the case of the federal surcharges, would have made for greater elasticity and independence in provincial finance.

The position of the States.—The position of the Indian States *vis-à-vis* the Federation and the Provinces is a somewhat privileged one, in this as in several other spheres.

So far as the indirect sources of central revenue, viz. customs, excise, and railways, are concerned, the States, or rather their subjects, bear a more or less proportionate share of their burdens. So far as direct taxation is concerned, however, the States have secured a twofold immunity for themselves. In the first place, ordinary income tax is not to be levied in the States, which means that there is to be no equivalent burden on the subjects of the States corresponding to the portion of the income tax retained by the Federal Government. One of the alleged foundations for this exemption is that the States are not responsible for the service of the pre-federation debt of the Government of India. Such an argument is faulty in as much as the new Federal Government has to inherit the strength, the goodwill and the credit of the old Central Government whose liabilities are to be offset against the much more valuable assets into the possession of which the States almost automatically enter. Besides, the burden of this debt is bound to be lowered in course of time and a perpetual exemption from income tax accorded to the States cannot be justified on what after all is a temporary burden.

The cash subventions at present received from the States are clearly unsuitable to their new status in the federation, and they are to be removed in a maximum period of twenty years, or earlier if the process of the sharing of the income tax with the provinces is completed before then. This is a very legitimate step, but equally legitimate would be the extension of the federal income tax to the States' territory. After the expiry of ten years from the inauguration of the federation the corporation tax is to be made applicable to the States. Why it is necessary to wait for ten years for this elementary law of uniformity of burdens to operate, and why, further, the States should have the option of paying lump sums through their Governments are very difficult questions to answer, except on grounds of the expediency of political bargaining. As a matter of fact, the abolition of subventions unaccompanied by a liability for income tax, and the provision of a definitely vague liability for the corporation tax, are measures which treat the States in a

markedly preferential manner which is inappropriate and unfair in a federation. The States ought to take their place along with the Provinces for all burdens and advantages of a common government. The federal ministry is not even empowered to call for relevant information from the States bearing on their liability to corporation tax. This is to be done by the Auditor General of the Federation, and an appeal to the Federal Court against the assessment made by the latter is to be allowed. The whole position is anomalous, financially as well as constitutionally.

If the federal union is an act voluntarily entered into by the States with a view to form a common government, with one central and several commonwealth Governments, it is impossible to understand either their own insistence on several special privileges or the British Government's readiness to accommodate them in these unreasonable demands. Side by side with the liability for pre-federation debt is the liability for financing the deficit provinces. The creation of these Provinces is decided upon for the more efficient administration of the areas concerned, which are as much a federal charge as any other. There are similar areas in other federations and part of the burden of their administration is shared by all members. The States can hardly claim exemption from income tax on the ground that State subjects earning incomes in British India either in public securities or in other businesses are bearing the income-tax burden. Such income tax, wherever paid, is in respect of earnings arising out of British Indian economy, and they do not absolve the State populations from bearing their proportionate shares of federal income tax in respect of incomes earned in the States. That the States maintain in some cases defence forces is also made out as an argument against their being called upon to bear their just share of federal taxation. It must be noted in the first instance that not all States do this, and secondly the military efficacy of State forces wherever they exist is not always a matter to be depended upon for even local defence, leave alone federal defence. It can, however, be conceded that with the formation of the federation the liability of the States

to maintain defence forces should cease. If the States desire of their own accord to maintain these troops they cannot claim exemption from income tax on that score.

The position of the States with reference to customs duties is even more anomalous. So long as the prevailing customs are comparatively low and arise mostly out of traffic directly affecting the State populations the continuance of these taxes will not materially affect either the finance or the administration of the federation. Even here, however, the replacement of duties, which are in the nature of provincial tolls, by an internal tax on sales or on shop keeping might be considered a suitable reform calculated to give greater economic homogeneity to the whole federal area. In respect of sea customs which hamper the economic union of the federation and which arise in a large measure out of trade with areas outside the States concerned, no convincing case can be made out to continue them as a privilege of the particular States. An appeal to past treaties is in this connection most inapplicable. The new relations between States and Federal Government are those of integration and not of alliance. The federation in respect of federal subjects supersedes all existing treaties, and though it ought to be really open to every State to make up its mind either to join the federation or not, it ought not to be made possible for any State to join on unfederal terms and thus to pervert and to sabotage the whole machinery of federal finance and administration.

CHAPTER XXXIII

LOCAL FINANCE

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I

Local expenditure in India and other Countries.—In 1931–32, the latest year for which consolidated statistics are available, local bodies in India incurred an ordinary expenditure of a little more than Rs. 22½ crores exclusive of the amounts falling under debt and other extraordinary items.[1] This gives an indication of the magnitude of the work they were in a position to undertake. Though this was more than four times the amount spent by them in 1894–95 and more than one-and-a-half times the amount spent in 1918–19, it should on the whole be regarded as a comparatively small expenditure, especially in view of its not having shown a tendency to increase perceptibly in recent years. It formed only 11 per cent of the total public—Central, Provincial and Local—expenditure of the country. The expenditure per head of the population came to Rs. 1–1–0, an amount too low to produce any really appreciable results when in its turn it had to be distributed among a host of items in the fields of health, sanitation, medical relief, education, roads, etc. In contrast to this, all the local authorities in England and Wales spent in 1929–30 a little over £425 million, which was nearly nineteen times the expenditure in India.[2] It came to more than 35 per cent of the total public expenditure and to £10 17s. per head of population. In 1929 local expenditure constituted 55 per

[1] Calculated from the figures in the *Statistical Abstract for British India*, 1934.

[2] Finer, *English Local Government*, p. 373.

cent of the total public expenditure in U.S.A., 50 per cent of it in Japan and 40 per cent of it in Germany.[1] It is clear from this that the services rendered by local bodies are more highly valued in the other leading countries of the world. And this is as it should be, because local authorities minister to those needs which directly contribute to social well-being. The State has in most countries been showing a tendency in recent times to be less and less an organisation for mere defence and police and to become more and more a social service corporation. Social services like the promotion of health, housing and education are traditionally associated with the work of local authorities and the transformation in the character of the modern State is being reflected in an increase of local expenditures. Conditions are quite different in India. At the rate at which local bodies are moving here it will take them a long time to approach the level attained in other countries. To hasten the pace at which local expenditures should increase is one of the immediate needs of the financial situation in India.

Its distribution among Corporations, Municipalities and Rural Boards.—The distribution of the total local expenditure may be examined from the territorial and the functional standpoints. Territorially, local bodies in India fall into three groups—the corporations, the urban municipalities, the rural district and other local boards. In 1931–32 there were 4 corporations (Madras, Bombay, Calcutta and Rangoon), 781 municipalities, and 1,247 rural boards. Twenty-five per cent of the total local expenditure was incurred by corporations, which meant a *per capita* expenditure of Rs. 22–3–0; 35 per cent was incurred by municipalities whose *per capita* expenditure came to Rs. 5–5–0; and 40 per cent by the rural boards with a *per capita* expenditure of only 7½ annas. In this percentage distribution there have not been large variations from time to time. Moreover, the *per capita* expenditure has always been highest in the corporations and lowest in the rural areas. The rapid growth of the *per capita* expenditure in corporations is in keeping with

[1] Article on Local Finance in *Encyclopaedia of Social Sciences.*

what has been observed in cities elsewhere. "Municipal government follows what economists call the 'law of increasing costs'—in other words the larger the city's population the greater is the *per capita* cost of serving this population."[1] The analysis, however, of the distribution of expenditure in India shows that the rural needs are not being attended to with the same interest as urban needs. Although the larger wealth of cities makes a higher *per capita* expenditure possible for them, the present distribution is so uneven that the financial system has to be remodelled with a view to bring about an improvement in the supply of rural services.

The functions of local bodies are grouped in official statistics under the heads of (i) Public safety, public health and convenience, (ii) Education, and (iii) Civil works, of which the construction and maintenance of roads and other means of communication form an important item. The significant omissions in this connection are poor-relief and police which occupy a prominent place among the functions of local authorities in the west. In India poor-relief is left entirely in the hands of private individuals and voluntary organisations; and the maintenance of police is a function of Provincial Governments. In 1931–32, 31 per cent of the total local expenditure was incurred on public health and convenience and 27·5 per cent on education, while the balance was utilised for civil works, general administration and several miscellaneous items. An analysis of figures for a series of years shows that while only 12 per cent of the total expenditure was incurred on education in 1894–95, it increased to 17 per cent by 1918–19 and 20 per cent by 1925–26. The expenditure on public health was 35·7 per cent of the total in 1894–95; it was 38 per cent in 1925–26, but it fell to 32 per cent in 1931–32.[2] The conclusion follows that local authorities have been placing a relatively greater emphasis on education and that public health has come to occupy the next place in their estimation. Separate figures

[1] W. B. Munro, *Municipal Government and Administration*, Vol. II, p. 444.

[2] Calculated from the figures in *Memoranda to the Indian Statutory (Simon) Commission*, Vol. V.

of expenditure on roads are unfortunately not available; but from the comments occasionally made by Provincial Governments in their annual reviews one gathers the impression that the percentage of expenditure on roads is on the decrease. It should, however, be noted that these conclusions based on averages for the whole country have to be made use of with a great deal of caution as conditions differ very much between Province and Province and between urban and rural areas.

Its distribution among the different functions of local authorities.—The distribution of expenditure among the various functions may be examined from the point of view of adequacy and effectiveness. Comparative rates of mortality may be taken as a rough measure of the adequacy of expenditure on public health. The death-rate per mille for British India in 1932 was 21·6 in contrast with 12 for England, 10·8 for U.S.A., 8·7 for Australia and 19 for Japan. The infantile death-rate per 1,000 births was 169 in India, while it was 65, 58, 41 and 132 for the other countries noted above.[1] An authority on comparative public health remarks that India still presents a picture like that of Europe in the Middle Ages and that in 1927 she reported to the League of Nations 350,000 cases of cholera, 58,000 cases of bubonic plague and 213,000 cases of smallpox—in each case far more than were reported by all the rest of the world put together.[2] It is true that local expenditure is only one of a number of factors on which the state of public health depends and that the exact relationship between the two should be determined more or less on the same lines as economists determine the utility of several complementary things which render services jointly in the production of a finished commodity. Even though an investigation of this sort has not yet been made, the high rates of mortality in the country justify the broad conclusion that local expenditure on public health is inadequate. To estimate the effectiveness of this expenditure it is necessary to enquire into the correlation between

[1] *Report of the Public Health Commissioner (India)*, 1932.
[2] Article on Public Health in *Encyclopaedia of Social Sciences.*

an increase in it and a reduction in the rates of mortality for a series of years. The fall in the general death-rate per mille from 34 to 22 and of infantile mortality from 208 to 169 during the period from 1911 to 1932 indicates in a general manner the effectiveness of local expenditure. To measure it precisely a closer scrutiny of the figures is necessary which it is not possible to carry out in this limited space. Such a scrutiny will also reveal the extent to which the expenditure was economical.

In the several reviews and reports on education published under official auspices from time to time a more detailed examination of the adequacy and effectiveness of educational expenditure has been made. The test applied in this case is the extent of literacy and the rate at which it is increasing. It is now recognised that on the basis of this test the educational expenditure incurred by local authorities should be pronounced to be both inadequate and ineffective. According to the census of 1931 only 8·3% of the population in British India was literate as contrasted with practically universal literacy in most of the other progressive countries. Critics have also pointed out that though the number of pupils in the elementary schools maintained by local authorities has been increasing more or less in proportion to the increase in their educational expenditure, most of the pupils are found in the first two classes only and that a large percentage of those that pass even through Class IV attain such a low standard of literacy that they relapse into illiteracy soon after they leave school. More than one-half of the amount spent on schools is thus a waste.[1] The introduction of a scheme of compulsory education is considered to be the only remedy to avoid this wastage. Even if it cannot be introduced universally it must be adopted in select areas. The consolidation of schools is another urgent need. The diversion of a part of the money now spent on ordinary schools to the promotion of adult education and village libraries will help to extend and keep up literacy and make educational expenditure more effective than what it is at present.

[1] *Report of the Auxiliary (Hartog) Committee of the Indian Statutory Commission*, p. 47.

Though in laying down a standard of adequacy in regard to roads the density of the population and the volume of existing and prospective traffic are to be taken into consideration, it may broadly be stated that compared with the advanced countries of the world the supply of roads in India is inadequate. In 1931–32 there were 240 miles of road for every 1,000 square miles of area, while the corresponding figures for England, U.S.A., Germany, and Japan were respectively 2,039, 1,017, 1,201, and 4,470.[1] The growing intensity of competition between the Road and the Railway has also revealed the ineffectiveness of the expenditure on roads owing to a high percentage of roads running parallel to railways within a short radius, and the absence of a well-co-ordinated plan of road construction.[2] The distribution of expenditure on the different classes of roads—metalled and unmetalled, district and village—is also found to be so much unbalanced that if the social utility derived from communications is to be at its maximum, funds now spent or proposed to be spent on trunk and district roads should be partly diverted to connecting the important villages with the public road system. Much of this ineffectiveness could have been avoided if the village had been recognised as the primary unit of local self-government and *panchayats* constituted to look after its interests.

It is a sound maxim of theoretical economics that funds available should be so distributed among the several functions of local government that the last rupee spent on any one function should yield the same amount of social utility as the last rupee spent on any other. But this maxim is so difficult of application in actual practice that differences of opinion are bound to arise as to whether local authorities are not spending too much on education and too little on public health and roads or vice versa. Provincial Governments in India generally entertain such apprehensions about the financial work of local bodies. For instance many of them have been complaining that enough money is not

[1] Article on Roads in *Encyclopaedia of Social Sciences.*

[2] Mitchell and Krikness, *Report on the Present State of Road and Railway Competition*, p. 7.

spent on roads.[1] To prevent what they consider to be wastage due to uneconomic distribution of resources, several measures have been adopted from time to time by Provincial Governments. In some Provinces legislation draws a distinction between the obligatory and the optional functions of the local bodies so that much may not be spent on the latter to the detriment of the former.[2] Statutes also lay down that the proceeds of particular taxes—the education tax, the drainage tax, the water rate—should be spent only on a particular purpose and not incorporated in the general funds of the local body concerned. Sometimes administrative orders are issued regulating the expenditure on particular objects. For instance it was a direction of the Madras Government for a long time that the expenditure on roads should be equal to the net income from tolls and one-half of the proceeds from the land cess. Similar standards were laid down by some of the other Provincial Governments also. Apart from the constitutional anomaly involved in thus fettering the discretion of autonomous local bodies, it may be noted that even financially such rules may not prove to be sound. Conditions vary from one local area to another in the same Province. One area may be in need of more roads, another of more schools. A rigid rule, therefore, may lead to extravagance and waste. A better device for regulating the expenditure of local bodies is the system of provincial grants-in-aid which may be effectively utilised to encourage expenditure in desirable directions. Fruitful advice may also be given by Provincial Governments when they review the annual administration reports of the local authorities.

II

Local revenue.—Local bodies in India derive their revenue from (1) taxation, (2) grants made by Provincial Governments, and (3) some miscellaneous items like fees and profits from remunerative undertakings. Of these the first two are at

[1] *Reports on the Administration of Bengal:* 1931–32, 1932–33.
[2] *e.g.*, The Bombay District Municipal Act, 1901, Ch. VI.

present the more important sources of their income, though their relative importance varies as between corporations, urban municipalities and rural boards. The following tables give an idea of the proportions which the income from taxation and grants bore to the total income of each class of local bodies in some of the years in the past.

Local Body	*Percentage of income from taxation in*				
	1894–95	1907–08	1918–19	1925–26	1931–32
Corporations .	63·4	80	78·4	80·5	72·2[1]
Municipalities .	60	63·1	51·8	63·2	
Rural boards .	57	48·1	48·1	52·3	42
All local bodies .	59·2	60·0	58·3	60·1	59

Local Body	*Percentage of income from grants in*				
	1894–95	1907–08	1918–19	1925–26	1931–32
Corporations .	1·5	2·6	·9	1·2	6·0[1]
Municipalities .	3·1	4·1	11·3	9·9	
Rural boards .	11·4	18	36·6	43·5	45[2]
All local bodies .	6·1	10	19·3	21·7	24[3]

It is clear from the above tables that corporations depend most upon taxation and least on grants from Government. Even in the case of municipalities, grants play a relatively small part. On the other hand rural boards tend to get less and less from taxation and more and more from Provincial Governments. This is to some extent explained by their comparative poverty and economic backwardness.

The taxes and rates levied by corporations and municipalities are of a varied character. They consist of (1) Octroi and its modification, the terminal tax, (2) a tax on houses and lands, (3) a tax on vehicles and animals, (4) a tax on professions and trades, (5) tolls on roads and ferries, and (6) some minor taxes like those on servants and pilgrims. It should not, however, be understood that the levy

[1] Separate figures are not available.
[2] Separate figures are not available.
[3] A rough estimate.

of all these taxes, is authorised in every Province. But the recognition of the principle that a number of taxes is better than a single tax is of much significance. This makes municipal finance in India similar to that which prevails in the countries on the continent of Europe. It secures the possibility that the defects found in any particular tax may be made up by the merits of other taxes; and when the whole tax-system is properly administered the burden becomes more evenly distributed among all the sections of the local community. Whether the multiple taxation in India actually produces this result is a question to which a brief reference will be made later.

Of the above taxes the first place is occupied from the point of view of the yield by the tax on houses and lands and the next place by octroi. In the table below is given in terms of percentage the proportion which the income from some of the principal taxes bore to the total income from taxation in recent years.

Name of the tax	1922–23	1925–26	1928–29	1931–32
Tax on houses and lands .	32·8	38·6	38·6	40·2
Octroi	19·9	15·4	13·7	11·7
Tax on animals and vehicles	3·5	3·5	3·5	3·3
Tax on professions and trade	3	2·7	2·5	2·4
Tolls	2·8	2·8	2·9	2·1

The balance of revenue from taxation was derived in these years from the minor taxes and from water, lighting and conservancy rates.

In rural areas the only important tax is the land cess or the local rate. There are a few other taxes like the profession tax in the Madras Presidency and Bombay, but the revenue from them is of an insignificant character. In 1932–33, for instance, land cess contributed about Rs. 85½ lakhs out of a total tax revenue of Rs. 86½ lakhs in the Madras Presidency and Rs. 47½ lakhs out of Rs. 50 lakhs in Bombay. The situation was not very much different in the other Provinces. Local taxation in rural areas is thus more like the English system where a single tax—the Rate

levied on occupiers of fixed property—is the source of all tax-revenue.

In examining any system of local taxation the essential points to be observed are whether it is really local and whether it conforms to what is generally understood by taxation. The need for a separate system of local finance rests primarily on the recognition that certain functions of government like sanitation, drainage, parks, lighting, etc., are primarily of service to the inhabitants of particular areas and that the funds required for their efficient administration should be contributed only by such inhabitants. It is unjust that the people of one locality should enjoy the benefits of service and that those of another should bear the burden of paying for them. A local tax is therefore truly local when its incidence is on the inhabitants of the locality concerned. As a tax it should be based on the principle of ability to pay. Some of the inhabitants should not be overburdened and others let off rather lightly. The defect with the Indian tax-system is that a few of the taxes included in it tend to prove burdensome to non-residents, while the system as a whole bears more heavily on the poor than on the rich.

This explains the reason why a good deal of controversy has gathered round octroi which is levied in a large number of municipalities in the Punjab, the United Provinces, the Central Provinces and Bombay and which yields a substantial proportion of their tax-revenue. It has been universally condemned as wanting in certainty, economy, convenience and equity.[1] As necessaries of life are not exempt from it, it produces a heavier burden on the poor than on the rich. It acts in many cases as a sort of transit duty interfering with the freedom of internal trade and consequently imposing burdens on the non-residents. It also prevents the Central Government from fulfilling some of the terms of the international conventions to which India is a party. It is therefore now agreed that the rates at which it should be levied should be kept low in all cases and especially so in the case of necessaries of life and articles

[1] *Memoranda to the Indian Statutory Commission*, Vol. V, pp. 988–96.

that are subject to imperial or provincial taxation; that arrangements should be made for prompt refunds on re-exported goods and for bonding those goods which are intended for through transport, and that the Central Government should have power to prohibit its levy on articles like sugar, matches, salt, kerosene oil, etc., on which heavy customs and excise duties are levied. Though recommendations on these lines were made so far back as 1926 by the Taxation Enquiry Committee[1] much effect has not yet been given to them. The only improvement that is now found is that the terminal tax—which is an octroi without provision for refunds and collected by railway authorities—is gradually taking its place in many municipalities. One of the disadvantages of octroi is that in some cases the refunds paid are much more than the amount originally collected.[2] A terminal tax does not suffer from this defect. It has also been found from experience that "improvement in trade proves more beneficial to municipalities with terminal tax than to those which adhere to the old system of octroi."[3] In spite of merits like these a terminal tax may prove as harmful and fiscally as unsound as octroi if precautions are not taken to prevent its being levied indiscriminately on all sorts of goods and on goods exported from towns. Other objections to it are that it sometimes operates as a surcharge on railway rates and that it necessitates the imposition of the vexatious toll on goods imported by road. Municipal finance will be considerably improved if both octroi and terminal tax are abolished and if they are replaced by a tax on houses and lands and a tax on professions and trades.

The tax on houses is one of the most widespread of local taxes in the world mainly because an improvement in the services of local government is best reflected in an increase in the value of house-property. The tax in India is mostly based on annual rental value and the question to be considered is whether it is a fair index of the ability of the

[1] *Report*, p. 298–99.
[2] *Government Review on Municipalities in the United Provinces*, 1932–33.
[3] *Government Review on Municipalities in the Punjab*, 1933–34.

tax-payer. To the extent to which the incidence of the tax is on the owner of the house, the rental value of it is not a correct measure of his ability as it does not constitute the whole of his income. Where it is the occupier that bears the burden of the tax, it imposes a heavier burden on the poorer occupiers than on the richer ones, as rents do not form a uniform percentage of the income of persons. It is a matter of common observation that the poorer a person happens to be the higher is the proportion of his total income spent on rent. There is no provision in any of the Acts now in force for a levy of house-tax on a progressive scale. One is led, therefore, to the conclusion that though as a tax the house-tax is local in character, as the burden cannot be shifted to non-residents, it does not completely satisfy the canon of equity. The same is true of the local land-cess in rural areas. It is ultimately based on the annual rental values of lands cultivated. The poorest ryot, however, has to pay at the same rate as the richest. Here also there is need for some kind of progression.

It follows from this that unless the above taxes on land values are supplemented by others which have a more direct reference to the income of all the residents in the locality the tax-system has on the whole to be pronounced to be regressive. Such is actually the case in the rural areas. Except in some of the areas of the Madras Presidency where a tax on professions and trades is levied, in the rest of rural India the many persons who do not own lands but who get income from other sources contribute nothing directly to local revenues. Even in the areas where the profession tax prevails, the machinery of assessment and collection is so inefficient that the yield from it is little and even that is gradually diminishing. When properly worked, it is just like a local income tax and can therefore serve as a corrective to the regressive nature of the tax on houses and lands. But it is not widely made use of by municipal authorities though a provision for it exists in almost all the Provinces. Out of the Rs. 31 lakhs which it yielded in 1932–33, Calcutta alone contributed nearly Rs. 12 lakhs, while the municipalities in Madras contributed

Rs. 12 lakhs.[1] The only tax that bears heavily on the rich is that on vehicles in towns, as the rate of the tax for the more luxurious class of vehicles is fairly high.[2] Thus, though the principle of multiple taxation is accepted in India it is not scientifically worked for the purpose of removing the defects found in particular taxes and making the whole tax-system an equitable one.

The regressive nature of local taxation may also be corrected to some extent by a system of State grants in aid of local authorities if it can be shown that the revenue of the Government which distributes the grants is itself based on ability to pay. In India local self-government is a provincial subject and grants-in-aid to local bodies are made by Provincial Governments which derive the larger share of their revenue from taxation of land and from excise which are also regressive in their operation. The value of provincial grants lies more in its strengthening of the local resources than in rectifying the inequitable character of local taxation.

It has already been pointed out that 24 per cent of the income of all local bodies and 45 per cent of the income of rural boards was derived in 1931–32 from provincial grants. In England such grants constituted about 20 per cent of the entire expenditure of local authorities in 1929–30.[3] Grants are made in India for general purposes, education, public health, roads and other civil works. Most of the functions discharged by local bodies have come to be regarded as semi-national services in which the country as a whole should take interest. All grants are made out of the general revenues of the Provincial Governments and not out of the proceeds of any particular tax. The only exception to this is the yield from the provincial motor-vehicle taxation in some Provinces which is distributed among the various local bodies to enable them to maintain roads. Most grants are given on a percentage basis, while there are block grants in a few cases. Grants are made not only to meet the recurring expenditure on maintenance but also towards

[1] Figures in *Quarterly Journal of the (Bombay) Local Self-Government Institute*, July, 1935.

[2] *Report of the Indian Taxation Enquiry Committee*, para. 452.

[3] Finer, *English Local Government*, p. 378.

capital outlay on water-supply and drainage schemes and on other public works. There are two anomalies in the distribution of grants. One is the failure to take into consideration the relative needs of the local bodies. Those which utilise their powers of taxation to the fullest extent and still remain in want are not treated better than those that fail to do so. The removal of this anomaly will increase the tax-income also of local bodies. The other anomaly is the possibility of securing special grants through the exercise of political pressure or influence on the provincial ministry. This leads to a certain amount of unfairness in the distribution of grants.

Fees are collected by local bodies in return for specific services rendered by them. Fees levied in educational and medical institutions, scavenging fees like those in Madras and the tolls levied on roads are of this character. Tolls used to produce a substantial income in Madras but they were abolished in 1931 on the ground that they impeded through-traffic and were felt to be vexatious by the owners of motor vehicles. A provincial tax on such vehicles was substituted but it did not yield the income expected of it. The mistake lay in abolishing the tolls on country-carts. The impediment to through traffic or the vexatiousness of the tolls does not apply to these slow-moving conveyances. Moreover they do irreparable damage to roads. There is now a move to revive the tolls on carts, and it will be a wise step on the whole, as there is no other equally good alternative for taxing them. Fees are also levied to regulate traffic in dangerous and offensive businesses like tanneries, laundries, etc. Whether licence fees like these should be made a source of income has become a matter of controversy although in some other countries they are so utilised.

One noteworthy feature of local finance in India is the small part played by commercial undertakings. In England and other countries a good deal of revenue is derived from water-works, gas-works, tramways, markets, and land-developments schemes. Even in India the Central and Provincial Governments run enterprises like railways, irrigation, and hydro-electric works. But local bodies have not

been forward in this direction. The only source from which they at present derive a substantial income is markets and slaughter-houses. A few district boards in Madras own railways but there is no possibility of any further expansion in this sphere as the Government of India has decided on a policy of centralisation. There is immense scope for undertaking bus-services, the supply of electricity, waterworks, tree-planting, housing and land-development schemes. Some of these are sure to bring profit and others are of great social utility.

Such a forward policy is possible only when local bodies resort to borrowing on a very much larger scale than they are doing now. Commercial enterprises cannot be started unless large amounts of capital are initially invested. This equally applies to non-commercial undertakings like roads, sewers, hospitals, school and office buildings, museums, baths and wash-houses. All these are sources of permanent utility and bring benefit to the tax-payers not only for one year but over a series of years. The expenditure on them should therefore be spread over a number of years, and that involves borrowing. It is neither fair nor practicable to finance them out of current income. But most local bodies in India have not been observing this distinction between expenditure to be met out of current income and that to be met out of loans. Even in a progressive Province like Madras the total debt outstanding against all urban municipalities and rural boards was only Rs. 239·63 lakhs at the end of the year 1932–33, which works at less than 9 annas per head of population. In England, which has about the same population as Madras, the outstanding debt in 1929–30 was £1,224·7 millions, which is equivalent to about £28 per head. A forward loan policy is therefore necessary if local bodies are to become more serviceable to the Public. It will also induce local bodies to make a fuller use of their powers of taxation.

III

Development of local revenues, the main problem.—The central problem in Indian local finance at the present day

is the discovery of ways and means for developing the resources of local bodies so that they may be in a position to discharge effectively the functions with which they are entrusted. The devices to be adopted for this purpose are partly administrative and partly financial in their character. But as a preliminary to all of them a change in the mental attitude of the people and their representatives in favour of taxation is essential The primitive prejudice against taxation by public authorities is a persistent obstacle in the way of any progress. The electorate should learn that there are circumstances in which social utility can be better promoted by public than by private expenditure. Such a lesson ought to be easier in the field of local than of imperial or provincial taxation, as the benefits accruing from expenditure by local bodies are immediate and direct. That the present level of local taxation is low[1] and that it should be considerably raised ought to become an article of faith with the electorate.

One important administrative step that has to be taken is the reduction in the number of local authorities in rural areas. In some Provinces there are as many as four authorities at present—a district board, *taluk* or sub-district boards, unions and village *panchayats*. This creates unnecessary financial complications and leads to wasteful expenditure on establishments and general administration. Indian conditions require only two authorities—a district board to be in charge of functions which in the interests of economy have to be carried on on a large scale and village *panchayats* to look after the other functions. The abolition of all intermediary authorities and the universal organisation of village *panchayats* will enable a better utilisation of local revenues.

The failure to recognise the importance of the village in the public economy of India has been a source of much harm. The setting up of a *panchayat* in every village will strengthen the willingness of the inhabitants to tax themselves and will also help in the revival of many traditional forms of taxation which have fallen into disuse. There are at present hundreds of villages which have been paying a

[1] *Report of the Taxation Enquiry Committee*, para. 454.

local cess for the last sixty years and more but which do not have a road or a school or a well in their neighbourhood. To create enthusiasm for taxation under such circumstances is an impossibility. The organisation of *panchayats* will give the villagers an institution which will devote its attention primarily to the welfare of the village. It can also revive some of the older sources of communal income and some forms of taxation like contributions in the shape of personal service, free cartage of materials and payments in kind. Moreover a small jurisdiction like the village will facilitate the assessing and collection of taxes like the profession-tax in regard to which a knowledge of local details is of the greatest importance.

The separation of the political from the executive functions of local bodies is another administrative reform required urgently. Elected local bodies and chairmen cannot resist the pressure exercised on them by the electorate and the more influential sections of the people. While such influence is not very injurious in the formulation of policy it is bound to be harmful and mischievous in the day-to-day work of assessing and collecting taxes. At present elected authorities are made responsible for carrying out these purely executive duties. Under-assessment, failure to revise assessment at frequent intervals, and leaving a large portion of taxes uncollected have become the normal feature of many municipalities and rural boards. Experience has shown that where the routine financial work is left in the hands of commissioners and executive officers enjoying permanence of tenure or of the members of the several provincial and imperial civil services, assessment and collection are decidely better. It is therefore necessary that the financial machinery should be entirely reformed either by the institution of a local civil service in each Province or by the provincialisation of the financial officers of local bodies.

Among the improvements of a directly financial character the first place is to be given to the need for the fullest utilisation of all the existing powers of taxation. There are many authorities in every Province whose rates of taxation

are far below the statutory maxima fixed by Provincial Governments. Moreover many local authorities do not care to levy some taxes at all. This applies to taxes on professions and trades and to those on circumstances and property. Where recourse is taken to them they are levied at different rates by different local bodies. The vast disparity that now exists between one neighbouring area and another in the matter of the incidence of taxation per head of population illustrates the failure of local authorities to utilise their financial powers to the full, even though the disparity may in some cases be due to differences in the wealth and income of the people concerned.

It is sometimes suggested that an addition should be made to the number of taxes that local bodies are permitted to levy. There is not much need for this in urban areas as there is already a provision for a variety of taxes in them. What is more necessary in their case is either the removal of statutory limits to the rates of taxation or at least the raising of those limits. In rural areas the only important tax at present is the land cess. It requires to be supplemented by a tax on professions and trades in all those Provinces where it is not at present permitted. A wholesome course will be to have a universal system of village *panchayats* and empower them—as is the case in Madras and to some extent in Bombay—to levy any tax suited to the locality with the previous sanction of the Provincial Government or the district board. This will be more flexible than giving them the power to levy particular taxes like a marriage tax or a tax on transfer of local property. For it is not easy to draw up a list of local taxes appropriate to small territorial jurisdictions. With the rapid growth in the means of communication it is becoming increasingly difficult to localise the source of a man's income, which, after all, is the measure of his ability to pay taxes. In most countries the tendency has been towards the centralisation of taxation and increasing provincial grants to local bodies. Decentralisation is possible only in the field of expenditure.[1]

The suggestion put forward that local bodies should get

[1] Article on Local Finance in *Encyclopaedia of Social Sciences*

a share of the provincial excise or of some other provincial tax is also not helpful. Experience of this system in other countries has shown that there is no guarantee under it that local authorities will get a continuously increasing revenue to meet their growing expenditures. It is better that any help obtained from Provincial Governments assumes the form of grants from general revenues without reference to the proceeds from any particular tax.

In almost all other countries of the world it is the local and not the Provincial or the Imperial Governments that levy taxes on land. In India it is the Provincial Governments that tax it and enjoy the proceeds from it. It is this more than anything else that is responsible for the inadequacy of local resources. The solution, therefore, of the financial difficulties in which local authorities are at present placed will be comparativly easy if they are permitted to tax land and the Provincial Governments give up their claim to it. But this is not within the realm of practical politics, as such a course would result in the bankruptcy of almost all Provinces. The compromise recommended by the Taxation Enquiry Committee[1] that provincial taxation on land should be standardised at 25 per cent of its rental value (instead of the theoretical 50 per cent of it) that local bodies be authorised to levy a surcharge not exceeding 25 per cent of what is taken by Provincial Governments, and that over and above this surcharge additional and special temporary rates for specific local purposes may be imposed appears to be the best alternative. It may be incidentally noted that local bodies in India are not enterprising enough to carry out special improvements and collect the expenditure on them by levying special assessments on those that are directly profited by such expenditure. There is also no systematic attempt to tax the growing unearned income from land in towns by means of duties on transfer of property as is being done, for instance, in the Madras Corporation. Reform in these directions will improve the local revenues.

There is also a strong case for an increase in provincial grants. The functions discharged by local bodies are of a

[1] *Report*, para. 107.

quasi-national character and without an enhancement of provincial contributions the more backward areas cannot be brought into line with the more progressive ones. While this view is theoretically sound it may not be easy to put it into practice unless Provincial Governments adopt a policy of retrenchment in other directions or impose additional taxes on the people.

The undertaking of remunerative enterprises will be another source of income to local bodies. There is a large field for this in respect of bus-services, electricity supply, water-works and land development. Their exploitation will not only bring additional income to local authorities but will also result in a better type of service to the public.

Improvements in the directions suggested above will increase the ordinary revenue of local bodies. They will then be in a position to adopt a more progressive loan-policy and make themselves more useful to the country.

CHAPTER XXXIV

REFORM OF TAXATION

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Principles of a sound tax system.—We have been taught for a long while that the canon of taxation *par excellence* is that of equality, faculty or ability. The ingenuity of authors has sufficed to prove that all these variant modes of expressing the main principle of sound taxation lead to the conclusion that a progressive system of taxation administered with the necessary caution, in a way not to jeopardise the life of the goose laying the golden or the silver egg, is the ideal to be aimed at by all respectable tax systems. In a few countries, where economic progress and political democracy have registered a steady advance, the ends of such progressive taxation have for the most part been realised. In a country with backward and unprogressive economic life the complex and elaborate instruments of direct taxation have been found to be particularly inapplicable. The nature of the taxing authority has also been found to influence the tax system in a very vital way, not contemplated in the simple enunciation of the orthodox doctrines of sound finance.

Practical experience of the working of financial systems has suggested that besides the principle of equality, which supplies a fair technique of the distribution of public burdens in an ideal State, there are two other vital considerations in respect of which the actual working of tax systems varies considerably. In the first place, as noted above, the nature of political authority has a very noticeable influence on the structure of both the revenue and the expenditure sides. As a celebrated Italian author, Antonio De Viti, puts it, all

systems of taxation prevalent in restrictive political Governments have a tendency to work in practice as monopolies conducted to the advantage of the holders of political authority at the cost of those who are excluded from a share in the control of the tax system. On the other hand democratic Governments tend to have more competitive or equalitarian fiscal arrangements, so that the burdens and advantages created by the tax system are more proportionately distributed.

The purposes for which the State raises its income have also a very close bearing upon the final effects of the various methods of taxation. Not only the elementary canon of economy but other more positive canons of practical guidance are now considered to be necessary ingredients of a sound and well balanced scheme of public expenditure. With reference to the objects of public expenditure, a threefold classification can be effected. That expenditure which results in only maintaining the framework of government including the tax-collecting departments, general administration, policing and justice, is clearly of a preservative character. It only maintains intact the social order that it is the primary function of every State to support. Expenditure that aims at improving either directly or indirectly the tone, and in the wider sense the productivity, of the community as a whole may be justly called developmental and productive expenditure. Not only civil works, but also education, agricultural and industrial assistance, medical and hygienic services fall in this class. Besides this expenditure which has the interests of the community as a whole for its objective, there is a class of public expenditure which aims at realising some accepted standard of relative equality in the distribution of wealth.

Even in intensely capitalistic countries a toning down of the prevailing inequalities of wealth and the use of the tax system as a legitimate instrument of social policy are now among the accepted commonplaces of finance. The minimum that the poorer classes in these countries expect is that in the advantages created by public expenditure they should enjoy a share proportionate to their contri-

bution to the State exchequer. In fact, however, by a steeply progressive tax system a large share of the income and the wealth of the richer classes is diverted to the State and is used to add to the amenities of the poorer sections. The extent of this redistributive aspect of public finance in each country, of course, depends upon the degree of industrialisation and of the realisation of a democratic consciousness. A sound tax system must now be judged, therefore, not only with reference to the observance or otherwise of the canon of equality, but also with reference to its monopolistic or equalitarian tendencies, its merely preservative or developmental expenditure, and its socially indifferent or redistributive purposes.

Predominance of preservative public expenditure.—The objects of public expenditure in India are predominantly preservative. Since the inauguration of the era of responsible government in 1921 the amount and the proportion of what might be termed developmental expenditure are certainly on the increase, especially in the Provinces. But even now the proportion of such expenditure is very small and there is a complete absence of redistributive or social expenditure. On the basis of the budgeted figures for 1936–37 the proportions of preservative and developmental expenditure in the Central and Provincial Governments might be put down at about 80 and 20 per cent. respectively. With the exception of a few grants to educational bodies like the Benares Hindu and the Aligarh Universities, to central research organisations like the Agricultural Research Council and to the Provinces for rural development, almost the entire central expenditure was of a preservative character. In the Provinces civil works, education, medical relief and public health, agriculture and industry are attracting more expenditure to themselves, though since the difficulties consequent upon the sudden fall in revenues caused by the great depression commenced the developmental services have suffered considerably. The following table will give a rough idea of the distribution of expenditure among the three classes of objectives in India.

Analysis of Public Expenditure in India, 1935–36

(*Crores of rupees*)

Preservative				*Developmental*				*Redistributive*			
Item	*Central*	*Provincial*	*Total*	*Item*	*Central*	*Provincial*	*Total*	*Item*	*Central*	*Provincial*	*Total*
Debt services	12	4	16	Civil works	2	8	10	nil	nil	nil	nil
General administration	11	10	21	Education, research, etc.	1	12	13				
Protection	50	18	68	Medical and public health	—	5	5				
Direct demands	4	9	13	Agriculture, industry, etc.	1	3	4				
Total	77	41	118	Total	4	28	32	Total	nil	nil	nil
Percentage of total expenditure	78·5				21·5				nil		

Vital need for Economy.—It must be admitted that the total expenditure in India relatively to the size and population of the country is very small and hence the proportion of primary expenditure is bound to be relatively higher. The small amount of expenditure is in turn due to the limited taxable capacity of the people. The nation as a whole is very poor, the number of rich persons and the size of their fortunes comparing very unfavourably with the corresponding classes in more industrialised countries. In view of the absolute paucity of public resources in India it is an obvious conclusion that economy in the true sense of the word should be the watchword of our expenditure. In fact, however, several fundamental facts of our political life obstruct the natural application of the canon of economy to our public expenditure.

Let us take the scale of salaries of superior civil and military services in India. The principle which for over a century and a half has governed these salaries may be stated as follows: to pay to a superior servant as much salary as will induce the best British recruit to come out to India, will help him to live in comfort and dignity and to retire with what must be considered from the Indian standpoint a fortune. In the bad old days when the communications between England and India were both risky and uncomfortable, and when the conditions of life in India were comparatively harder, the inducement had to be really high. The traditions of private trading and other illegal gratifications which had been bequeathed to the statutory civil service by the East India Company's cadets had also to be counteracted by a substantial scale of regular payment. All these factors have now changed completely and there is no reason whatsoever why the scale of salaries should not be adjusted to the prevailing rates of payment for similar talent employed in non-official pursuits in India.

In this respect there is a primary consideration which is purely political in character. Must we continue to recruit a certain percentage of British servants, and if so, should the scale of payments to Indian members of a superior service be the same as that of British members? At any rate for the civil services immediately, and for the military

services in a short specific period, recruitment of foreign personnel might be rendered unnecessary, if the suitability of personnel is the only consideration. But the pace of Indianisation of the superior services, their composition and payment are matters which are beyond the control of the Indian Legislatures. The Indian members of the superior services are certainly the equals of their British colleagues in point of talent and devotion, and hence their claim to equality can hardly be resisted. All the same, under the new political dispensation, wherein a spirit of service rather than a mere professional loyalty might more naturally characterise the Indian superior servants, a differentiation in salaries might appear to be less inappropriate. As the salaries and allowances of ministers themselves are being drastically reduced a new outlook on the salaries of officials might now be practically effective.

With our limited public resources and with the prevailing low scale of earnings in the country we ought to pay our public servants a salary which will be no more than that necessary to attract and keep men of the requisite competence and integrity. The present scale of payments beginning at about 350 Rs. per month and ending in the normal course at about 2,000 Rs. excluding selection posts and allowances, is too far out of keeping with Indian standards. An initial salary of about 200 Rs. rising up to 500 Rs., with necessary allowances, ought to suffice to draw and keep efficient and devoted employees in the service of the State. If the competitive effect that the inordinately high scales of Government salaries are having on some non-Government jobs is withdrawn there is every reason to believe that the class of persons from whom the superior services are being recruited in India to-day will not consider the new scales of pay unattractive.

Machinery of Government.—In the military services the employment of British troops in India and the predominantly non-Indian composition of the officers' ranks are matters governed by political policy. Admittedly the economic loss directly caused by this policy is very great, and obstructs the application of the fundamental law of economy to our public

expenditure. With regard to the organisation of our system of administration the wholesale introduction of elaborate and costly English models has been a disaster, at any rate financially. Whether in construction or in organisation and staffing, we must keep the Indian needs and capacities constantly in mind. The functions of modern Governments are so extensive that some degree of centralisation and elaboration is inevitable. But the ruling bias of Indian administration ought to be towards decentralisation and simplicity. A breaking up of divisional commissionerships and the decentralisation of functions so as to make local authorities such as village, district and municipal bodies effective instruments of government, and not merely spending committees as at present, will go a long way in initiating the new orientation in our political structure and its economic costs. This is a matter which might attract the attention of the new responsible provincial administrations at an early date.

Tax burden on the poor.—Besides being exorbitant and wasteful Indian public expenditure is also unjustly distributed among the several classes of the community. By means of high salaries and allowances the foreign and Indian personnel of superior civil and military services get a first share in it. Other expenditure also is so organised as indirectly to contribute to the amenities of the superior servants and their dependants. Take as an instance the establishment of medical services in district places and the utter neglect of the countryside in this regard. Most of the so-called beneficent services of the Government in India originally started as aids to the European population and their dependants. In course of time as the urban educated class became more and more vocal these services were extended so as to reach them in some measure. But the poorer and rural classes of the community who bear the principal burden of taxation have always got a very small share of these services. Not only is there no redistributional expenditure in India, on lines of similar expenditure in other countries, such as poor relief, national insurance and efficient medical and educational services, but it is a plain fact that such redistribution

as the tax system does bring about in India is in favour of the richer classes. This constitutes a double wrong, as the system of taxation and of expenditure are both regressive. The table overleaf will give a rough idea as to how much is being taken from the poorer sections of the population and how much is being spent on them.

Rural versus Urban.—Even as a rough indication of the distribution of the advantages and disadvantages of public finance among the rich and the poor the table and the figures are eloquent. A further analysis of our principal sources of revenue and the disposal of expendable funds will show that a very small part of the latter is spent in the rural areas while a large part of the former is collected there. Apart from the very pressing need of economy and reorganisation in our system of expenditure, nothing is more vital to imparting health and justice to the whole scheme of finance than following a deliberate policy of spending more and more for the poor man and for the villager. The improvement of sanitary and medical services in rural areas, the spread of general and professional knowledge which will help the poor to help themselves by becoming more efficient producers, the improvement of agriculture by all kinds of State-directed and subsidised schemes, with which the recent history of even industrial countries abounds, the introduction of a vigorous campaign for better housing among the factory labourers, and the initiation of some schemes of national insurance such as sickness and unemployment benefit under suitable conditions, are channels through which the uneven balance of our public expenditure can be redressed. Part of this proposed additional expenditure can no doubt be financed by moneys saved by retrenchment and reorganisation. If political and constitutional difficulties prove too strong for this badly needed course of reorganisation and retrenchment, added sources of revenue must be discovered. Fortunately it so happens that the other end of the tax system also needs to be redressed by making the rich and the middle-classes bear their proportionate burden. In the meanwhile the Provincial Governments may well set up Committees on Public Expenditure to find out what can

Distribution of Revenue and Expenditure among Rich and Poor (1936–37)

What the Rich pay and receive (*crores Rs.*)				*What the Poor pay and receive* (*crores Rs.*)			
Burdens		*Advantages*		*Burdens*		*Advantages*	
Customs	37[1]	Interest	8[2]	Customs	18	Civil works	7
Salt	2	Civil works	4	Salt	7	Justice and police	10
Land revenue	4	Protection	48[3]	Land revenue	30	Education	10
Excise	1	Education	2	Excise	13	Medical	3
Stamps	2	Medical	3	Stamps	10	Agriculture	2
Taxes on income	16	Administration	18[4]	Forest	2	Industry	1
						Administration	3
Total	62	Total	83	Total	80	Total	36

[1] By a careful estimate of the probable consumption of articles bearing customs and excise duties it is worked out that about two-thirds of the total burden is borne by the rich.

[2] About half of the total interest payment is made within the country.

[3] The normal policing and magisterial organisation is what the poor man is interested in. The defence of the existing regime and mode of the system of civil judiciary is really in support of the claims of the richer classes.

[4] A large part of the expenditure on administration is remitted to England by English members of the services.

be done to make the existing resources go a longer way towards promoting the welfare of the taxpayers than they at present do.

Taxation of income.—No tax system in the world is perfect, but the Indian variety of it has more than its normal share of blemishes. That some of these are the outcome of the comparatively undeveloped nature of the nation's economy is undoubted. The general paucity of resources, the large proportion of primary to total expenditure and the undeveloped system of direct taxation are instances in point. At any rate it can be said with some assurance that the burdens of taxation in India, with the exception of the land revenue, do not bear heavily upon production. The pitch of the income tax is by no means very high, and the steepness of the scale of progression has often been criticised as being too low. The minimum limit of taxable income, that of 2,000 Rs., is very high considering the general level of Indian incomes. It is perhaps true that the assessment and collection of income tax from a large number of small assessees is more troublesome than the yield would justify. Perhaps the avenues of evasion are also liable to increase as the level of incomes is reduced. But it is a fact of general observation on which most inquirers into the subject have commented, that the non-agricultural middle classes, the petty business and professional men, escape their due share of direct taxation. If it is considered that smaller incomes are not suitable objects of an elaborate income tax, the tax on professions should be introduced in the Provinces at an early date. For most businesses and professions the issuing of a licence should be made obligatory. This will render a better regulation of professions feasible, and if an element of progression is introduced in the licence fees a very necessary tax reform will be effected. For the comparatively bigger business houses a turnover tax should be levied in addition.

As it is, the income tax cannot be said to be so stiff as to discourage production. In fact not only do the rates require an overhaul for steepening the progression of intermediate incomes, but such known methods of evasion as

differentiation between the income of the wife and the husband and the manipulations of incomes earned abroad must be rendered ineffective. Advance in these directions was recommended by the British experts brought out by the Government of India, and their recommendations have been adopted by the Government and by the Legislature. The taxation of agricultural incomes through income-tax is a matter now resting with the Provinces. If a substantial minimum limit of taxable income is to be laid down, this tax will more usefully apply to the landlord Provinces than to the *rayatwari* ones. Even in the *zamindari* Provinces, it is only in the permanently settled tracts that really large incomes, not properly taxed otherwise, are likely to be found. The legalistic difficulties associated with a proposal to tax the income of the great *zamindaris* have hitherto proved insuperable, mostly because the British Government in India would not consider it expedient to undo what a former Governor-General had done for a political as well as a financial purpose.

The provincialisation of agricultural income tax and the establishment of responsibility in the Provinces have changed the whole perspective of this problem. On the one hand the need for enhanced revenues is very urgent in the Provinces and especially in Bengal. A people's Government, moreover, can more appropriately weigh the relative claims of social policy and historical privileges than a foreign power. It is encouraging to note that a Committee was appointed in Bengal to inquire into the whole problem, legal and financial, created by the permanent land settlement. In due course, and with the necessary precautions as to the gradual liquidation of vested interests, not only the application of an income tax to agricultural incomes but the virtual withdrawal of permanent settlement, by conferring wide rights of taxation of land upon local bodies, will have to be effected. The incomes of agricultural intermediaries, which are in the nature of money paid by the cultivator for a purely functionless proprietorship, must be subject to a greater taxation than they at present bear. This is a measure of fiscal and social justice which ought

to be taken up at an early date not only in the permanently settled but in all Provinces.

Besides the liquor excise, which is supposed to act as a check on consumption but in practice fails to do so, and the salt excise, which is a revenue monopoly of the Government of India, the other excise revenues are match excise, sugar excise, the tax on kerosene and motor spirit, and the excise on steel ingots. The producing interests have in all these cases raised a protest against these excises and there is a considerable amount of uninformed sympathy expressed with this protest by people who suspect in these taxes a veiled opposition to Indian industrialisation on the part of the present Government of India. Evidence of production, consumption and prices, however, fails to justify any such feeling. Undoubtedly a part of these excises gets spread over the consumers, especially on the poorer classes who have to pay a more than proportionate share of the total yield. But neither total production nor normal profits in any of the industries concerned have been adversely affected. Wherever, as in the case of sugar and matches, the articles are the products of a protected industry the height of the tariff has been so adjusted as to take account of the excise. The consumers have some justification for grumbling against these excises, but the producers have hardly any. The total yield of the several excise duties as estimated for 1936–37 were as follows:—

Item	*Crores Rs.*
Excise on Matches	2·10
,, ,, Sugar	1·96
,, ,, Kerosene	3·00
,, ,, Motor spirit	6·00
,, ,, Steel ingots	·34
Total	12·40

Not only are the above excises not restrictive but there is reason to believe that the general revenue tariff, which in most cases is now at 25 per cent *ad valorem*, is having a protective effect in unsuspected quarters. A special inquiry into the whole working of the Indian tariff is now opportune. Not only the methods of discriminating protection

but those of indiscriminate revenue tariffs require to be inquired into, with a view to making deliberate protection more speedy, adequate and secure than at present and at the same time drawing to the public treasury by means of excise the part of producers' earnings which is created by the high revenue tariff.

The System of land taxation.—The tax that really presses on production in India is the land tax. Even here the strict theory of the land tax is that it is a tax on rental value, and thus is not in any way a burden on the cultivator. Even in the days of Lord Curzon the declared policy of Government was not to take more than half of the rental value of land. Since the days of Lord Curzon the proportion of the land tax to rental has in practice varied, due mostly to price fluctuations. But the theoretical limit also has been lowered from 50 to 40 in some Provinces, and an actually lower limit is by no means rare. The real source of hardship arises firstly from the great practical difficulty of deciding upon the amount of rent, and secondly from the undifferentiated and generally unprofitable nature of the cultivator's business. In most areas where a periodical revision of the revenue settlement is made rental values have to be estimated. In doing so the procedure is based upon the empirical observation of prevailing rentals, land values, price changes, improvement in population and transport, and similar factors. No attempt is made to base the settlement primarily upon the producer's surplus which ought to be the real measure of rent in this connection.

At first sight it might appear that nothing is more natural than to take the prevailing rental and sale statistics as the basis of estimated rents in a given area. As a matter of fact, however, this procedure is vitiated by some factors peculiar to Indian economy. Traditionally the possession of land and the business of farming have acquired in India an exceptionally high value, which is not justified from the purely economic or productive standpoint. What the land tax aims at hitting is the net product of land, and not the sumptuary or social value that people are prepared to

pay for its possession. In the second place the overstocking of agriculture and the large demand for the possession of land result in an enhancement of contractual rents, though an analysis into the costs of the agricultural business would show the relative absence of a surplus. Inquiries into the accounts of farming in several areas have proved conclusively that the capital invested in agriculture does not earn the return which it earns in other businesses, even when allowance is made for the comparatively secure nature of the former. The earnings of labour employed on land cultivated by the labourer himself are often lower than similar labour employed on hire.

This paradox between unremunerative agriculture and high rents is obviously the result of the relative scarcity of land. But when it comes to taxing scarcity rents, which are, at least in a *rayatwari* tract, merely conceptual rents, regard must be had in some measure at any rate to the taxable capacity of the payer. In this respect an analysis of the shares in the national dividend based on purely theoretical grounds may not, and in fact does not, coincide with facts. The shares of land, capital and labour, not to mention enterprise, constitute a composite total for a large portion of the Indian peasantry, and any tax which is theoretically levied on any one of these factors tends to fall on the rest. Care must, therefore, be taken to see that an already unremunerative industry is not rendered further unattractive to the investment of capital and enterprise by a too heavy taxation.

It is, indeed, necessary to see that trusting too exclusively to the concept of rent as unearned income we do not really levy a toll on the poor earnings of agricultural labour. Equally well the theory of taxable capacity cannot in its crude form be applied to the Indian land tax, at least for two sound reasons. In the first place, the scarcity rents, where they are paid, are definitely an outcome of social forces and their comparatively stiff taxation is justified as much on financial as on social grounds It must be suggested in this connection that a differentiation of revenue demand as between land cultivated by the owner himself and that

hired out on lease is quite a justifiable and feasible reform. A standard rate being fixed, a surcharge should be collected from landholders who have leased out their land. The details of this reform will have to be so worked out as to minimise the prospects of a transfer of the burden to the cultivator and of the discouragement of genuine investment of capital in the agricultural industry. The principle, however, of differentiating between the burdens on owner-cultivated and tenant-cultivated land should be immediately accepted.

In a country like India where the principal industry of the people is agriculture it is inevitable that a large proportion of the burdens of public expenditure should fall upon the agriculturists, irrespective of the productiveness or otherwise of their occupation. Where the whole of the nation's economic endeavour is relatively unproductive all the population has to share the burdens proportionately to their place in national economy. It is quite justifiable to argue that the non-agricultural occupations which are more productive, or less unproductive, should bear a higher rate of taxation. In applying this canon, however, care must be exercised to see that enhanced taxation does not kill the trade altogether, in the same way as land revenue must be so designed as not to push land out of cultivation. But the mere fact that a landholder does not pay his way is no proof of the absence of taxable capacity. Taxable capacity may arise out of a surplus where economic production as a whole results in a national surplus. But where the economy is one only of want and not of a surplus, taxable capacity has to be measured by total production, rather than by individual profit.

As between the several holders of land it is only proper that the total burden should be distributed in proportion to the productivity of each holding. Various elaborate schemes of ascertaining the gross and the net yield of land are now operative in the Provinces. Most of them suffer from two almost inevitable drawbacks. From experiments or observations in a very small number of cases generalisations and averages have to be worked out for the

whole area. With the best of methods and intentions in the world this is a procedure that must involve a considerable margin of error, which is bound to cause hardship. In the absence of any systematic and reliable accounts of farming the settlement staff has to exercise in so many respects what amounts to personal discretion. It would be most strange if in a revenue-minded staff this discretion did not usually err on the side of excessive rather than moderate demand. The dependence of Indian finance on land revenue is even now very great and was very pronounced in pre-war days. The burdensomeness of the land tax in several areas has arisen out of an inherently inefficient system being administered by parties who were the least competent to exercise an independent judgement.

Anything that simplifies and regularises the settlement procedure is bound to prove a welcome reform. The placing of the whole of the land revenue system on a statutory basis is of course the first step and will undoubtedly be taken by the new Legislatures. The lowering of the maximum pitch may also be attempted in a few cases. A more important reform of procedure is the association of the representatives of the taxpayers with the settlement officers while the process of settlement is going on and the provision of an independent tribunal to hear appeals for alleged excess. Even with all these reforms, however, the land revenue system is bound to remain imperfect on account of the inherently unorganised and unproductive traits of our rural economy. The improvements in technique and the elaboration of procedure are further calculated to prove costly and vexatious. In view of these basic defects of land revenue organisation it may be suggested that after a preliminary inquiry into the worst cases of excessive land revenue demand the present settlements should be declared to be permanent, subject to the following provisions. The money equivalent of land revenue should bear some correlation to a basic price level and striking variations in the price level should be reflected in the money demand on account of revenue.

In cases of emergencies it should be possible for the

Provincial Governments to levy surcharges on the revenue demand and these should last only for one year, so that the Legislature has an opportunity every twelvemonth to decide whether the extraordinary taxation is necessary. Any normal taxation of land on the part of the Provincial Governments should be confined to the levying of an income tax applicable to incomes above a prescribed minimum. Except for emergency surcharges and income tax on high agricultural incomes the Provincial Governments should deny to themselves the right to tax land any further than at the present rates, which should be stabilised. Local bodies like the *panchayats* or union or *taluk* boards which are more directly representative of the landholders and which have a closer contact with the conditions in the rural areas should be empowered to levy a rate on land either on the basis of its capital or rental value. Such a scheme of reform is calculated to make for economy, elasticity and justice.

Taxes on commodities and services.—With the exception of the income tax, which is paid exclusively by the rich and the higher middle classes, and the customs duties, of which the rich can be said to bear at least their due share, all the other important taxes in India have a tendency to bear more heavily on the poor than on the rich. The need of growing revenue in a country of small incomes and unorganised industry can be met more easily by resorting to indirect than to direct sources of income. The temptation to prefer the less obvious course of taxing commodities and services rather than persons is all the greater when the taxing authority is not popular in its composition, nor has the strength of conviction that can arise only by a thorough identification of objects between the taxing authority and the taxed. The recent history of Indian finance is freely sprinkled with fresh additions to taxes on commodities and services. The already regressive character of the tax system has been considerably accentuated by this development and unless determined efforts are made by the new Governments to initiate measures of less indirect taxation and to compensate the overtaxed

sections of the community by suitable expenditure on public services, the longstanding defects of the tax system will be perpetuated.

Taxation levied by the Central Government is already so extensive that any fresh impositions, even for corrective or developmental purposes, can only be thought of in connection with the Provinces. Out of the list of taxes which under the new Government of India Act are to be levied by the Central Government but are to be distributed among the Provinces succession duties on non-agricultural property are the most important. Commercial stamps are already levied by the Central Government, though the proceeds go to the Provinces. Terminal taxes are so vexatious that they cannot be thought of except in emergencies. The succession duty is a levy on property which is justified both as a measure of taxation, because it will correct the balance of burdens in favour of the poor, and also as an instrument of a mild redistribution of wealth. The introduction of such a tax in India will, however, be a very far-reaching step in legal and financial procedure. Important political parties who in course of time hope to have the control of finance in their hands ought to declare themselves on this question and to have their concrete proposals canvassed in the country before the measure is formally adopted. The graduation of this tax according both to the value of property and the degree of relationship would be desirable. But in view of the system of multiple sharers prevalent in India, graduation according to relationship of the inheritor would be very difficult and comparatively unproductive. Hence the levying of the succession duty should take the shape of an estates duty, so that the entire estate inherited by a multitude of heirs is taxed at the very source.

Income tax on non-agricultural incomes, salt and other federal excises and export duties belong to the category of centrally levied incomes which can be shared with the Provinces if the Central Government finds it possible to do so. In view of the straitened position of the Central Government there is little prospect of an early extension

of the system of sharing as it obtains now. In fact an addition to central excises, as, for instance, on tea, and even on cotton goods, is by no means unlikely and when it comes about the proposal to institute further sharing with the Provinces may become more practicable. In the meanwhile the policy underlying the salt tax is likely to come in for severe criticism under the new constitution. If the new legislators do not allow themselves to be swept away by a wave of sentimental opposition, to an old but politically unpopular tax, a rational way to deal with the salt tax would be so to adjust it as to establish an optimum of *per capita* consumption. If we study the figures for *per capita* consumption of salt in India when the duty on salt has varied we shall find that a figure of about a rupee per maund would by no means be a heavy burden. The objection to the salt tax is not that it is a burden on the poor, because there are so many others such as judicial stamps, which are even more onerous. It is only the tendency to consume less salt than necessary when its price rises that is disquieting. If the salt tax is lowered sufficiently to stabilise the *per capita* consumption at the desired figure, it will remain as a useful and elastic source of public revenue to be intensively utilised in emergencies. The following table of *per capita* consumption of salt will be found interesting in this connection.

Salt Consumption in India

Period	*Rate of duty per maund*	*Per capita consumption (lbs.)*
1903–05 . .	2 Rs.	10·6
1905–07 . .	1 Re. 8 As.	10·8
1907–16 . .	1 Re.	11·9
1916–23 . .	1 Re. 4 As.	13·0
1923–24 . .	2 Rs. 8 As.	11·9
1924–29 . .	1 Re. 4 As.	12·6

Another source of central revenue which calls for comment is the customs tariff. An indiscriminate revenue or protective tariff is bound to cause obstruction to normal movements of trade and to come up against the law of decreasing

returns sooner or later. Further still, the success of a protective duty lies in its extinction as a source of revenue, inasmuch as it is designed to check imports and not to enhance State income. It cannot, however, be argued from this obvious truth that the adoption of a policy of even sober, that is discriminating, protection is bound to reduce the yield of the customs very markedly. In fact the success of discriminating tariffs would lie in an enhanced yield from customs, excises and income tax. The development of industry entails the use of many producers' and semi-producers' goods and protection acts as an incentive to increased imports in this class. The establishment of one major industry leads to that of many other allied ones, which also import foreign material. The general enhancement in purchasing power and in the standard of the people, caused by a discriminating protection, also raises their demand for a miscellaneous assortment of goods, many of which have to be imported from abroad. The experience with the Indian customs since the introduction of a policy of discriminating protection has shown conclusively that though individual items, especially protective duties, are liable to a diminishing tendency and though in individual years owing to factors affecting international trade as a whole the yield of the customs is liable to shrink, the customs definitely improve with an improvement in business conditions and in the standard of life of the people. Protection must indeed be discriminating, and the operation of each individual item of the tariff must be closely watched by the experts of the revenue board. In this connection a more elaborate and if need be a more specific customs tariff, both revenue and protective, than the present one may prove more appropriate. But there is certainly no incompatibility between a policy of discriminating revenue and protective tariff on the one hand and of an expanding customs revenue on the other. The following figures taken from the financial statement of the Government of India for the year 1936–37 will be of interest in this connection.

Details of Import Duties.

(Lakhs of Rs.)

Item	1932–33	1933–34	1934–35	1935–36 *Revised*	1936–37 *Budget*
REVENUE DUTIES.					
Liquors and wines.	220·92	226·00	226·11	234·00	241·00
Fuel and lubricating oils	34·30	39·59	42·14	45·00	48·00
Motor-cars	68·10	95·02	133·69	130·00	140·00
Electric bulbs	18·06	15·92	16·60	18·00	20·00
Wireless apparatus	2·55	4·09	7·83	10·00	12·00
Machinery	127·86	150·86	159·71	172·00	180·00
Metals (other than iron, silver and tin)	92·10	75·86	96·05	100·00	105·00
PROTECTIVE DUTIES					
Sugar	684·79	472·04	381·35	360·00	200·00
Heavy chemicals	4·48	·18	·23	·15	·15
Iron and steel	110·37	85·05	78·60	75·00	70·00
Paper and stationery	21·71	24·24	21·26	23·00	23·00
Silk and silk yarn	49·70	29·93	50·77	55·00	55·00
Cotton fabrics	652·64	460·66	545·64	535·06	540·00
Matches	·41	·30	·23	·06	·00
All imports	4190·39	3568·36	3884·33	3884·00	3819·00

Field for Reform.—The really important field for immediate action is, of course, provided in the Provinces. Here, next to land revenue, excise on liquor is the most important source of public income. The traditional policy with regard to this tax was that almost all Provincial Governments professed to raise the maximum revenue with the minimum of consumption. Of late there was a slackening in the strict working out of this policy, and indeed in some quarters there was a definite tendency to raise higher revenue by improving the facilities of consumption. Recently the Congress Provincial Governments adopted a definite policy of prohibition. In this respect the financier is at the mercy of the reformer and the legislator. If a sufficiently large number of electors feel very strongly on this subject and if their representatives in the Legislature and the Government feel themselves to be sufficiently resourceful and efficient to enforce prohibition there is nothing to stop them from legislating for the abolition of drink and with it the excise revenue.

Apart from the purely moralist's standpoint, however, the legislator and the administrator must bear in mind the financial implications of their action. American experience of a similar measure has proved once again that legislation as a measure of social and moral reform is a weapon of limited usefulness, and that it can be used only as a supplement to moral propaganda among those who are primarily affected by an evil. In the absence of a successful campaign of moral reform among individuals and communities affected by the so-called drink evil, any legislative prohibition will not only obviate a very important source of provincial revenue but will definitely increase the costs of the administration by the necessity of maintaining a very costly preventive and policing staff. The opportunities for illicit distillation in India are so great that even a costly and efficient staff will not be able to stamp out the major portion of illicit distillation. The existence of a multitude of provincial and state borders will complicate the difficulties still further. Unless, therefore, the would-be prohibitionists exercise sufficient caution and exhibit the necessary amount of patience there is every danger of the Governments abolishing the excise revenue without really abolishing the drink evil. If, however, some of the Provincial Governments do enter upon an intensive policy of prohibition the financial difficulties of the Provinces will be accentuated. All the possible sources of revenue such as an agricultural income tax, succession duty with reference to agricultural property, occupational taxes, entertainment taxes, and even poll taxes may have to be exploited. These will affect all classes, and if the community as a whole is sufficiently keen on the abolition of the drink revenue they must be prepared to pay the price.

Local Finance.—The financial difficulties of local bodies have not hitherto attracted the attention that they deserve, owing mainly to the fact that the Central and the Provincial Governments have themselves been the centre of a good deal of financial interest. Recently there has been a welcome tendency to increase the functions of the local bodies. Both for the sake of administrative convenience and for the greater

realisation of the principle of self-government and local responsibility a further extension of this tendency is to be devoutly desired. But the same antithesis between expanding functions and stationary or shrinking revenues as was mentioned in connection with the Provinces is to be noticed with regard to the local bodies. Their sources of income are so limited that they cannot do justice to any of their present functions, leave alone the more vital and costly functions like policing and justice that may in course of time be delegated to them. Unless the provincial revenues gather greater financial strength than at present a policy of earmarked grants to local bodies will not be opportune. All the same, progress must be deliberately guided in the direction of decentralising the execution of functions. This will not only make for local responsibility and political training but also for considerable economy, if the utilisation of local talent, on a part payment or honorary basis, is practised on a much larger scale than at present.

Before a Provincial Government launches any far-reaching reform affecting the revenue or the expenditure it must frame a comprehensive scheme of reorganisation and consequential change in the financial and administrative spheres. Any piecemeal action in the financial sphere is likely to make for financial disaster from which several young democracies have in the past suffered. In any such scheme of financial and administrative reorganisation the strengthening of the competence and resources of local bodies must occupy an important place. Besides the sources of direct and indirect revenues that the local bodies at present possess they should be permitted to levy a graduated tax on agricultural property and on non-agricultural occupations, especially those of petty traders and money-lenders. The practice of collecting taxes in kind and making disbursements in the same fashion might be partially introduced at this stage. Local variety and local freedom of action ought to be promoted. An elaborate and costly system of administration will be unsuitable for our local, and especially for our rural, areas, as much in the political as in the financial fields.

CHAPTER XXXV

PUBLIC DEBT

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I

General features.—The present amount of the public debt of India is about 1,000 crores of rupees (March 31, 1935). This is the amount which the State has borrowed from private owners of capital under definite terms. Its total obligation is, however, much larger, the State being indebted to the public for deposits received at the Post Office Savings Banks, Cash Certificates issued, several provident funds maintained, and provincial balances administered. This sum amounts to Rs. 235 crores and should not constitute public debt in its strict sense. Funds are also raised by the Secretary of State by issuing debentures through the railway companies working State lines, the interest of which is guaranteed by him. Strictly speaking, the public debt of India should also include the debts of the Provincial Governments totalling a few crores of rupees; but this amount has been excluded from our discussion here because it is of minor importance.

The Indian public debt is held both in India and in England. The Indian portion consists of rupee loans raised in India, and the portion in England consists of sterling loans raised there. The difference between the two is not only in location but also in units of value, which introduces a number of distinctive features in the two branches of the Indian public debt. At the close of the financial year 1934–35, the rupee portion amounted in round figures to Rs. 487 crores and the sterling portion to £384 millions, *i.e.*, Rs. 510 crores when converted at the present statutory parity. The two portions

of the debt are thus almost equal. That should not lead to any rigid conclusion that the origin of the capital is equally distributed over the two countries or that the nationalities of the creditors can be equally demarcated. To-day the mobility of capital is so high that under the present advanced state of Indian credit not only foreigners invest in the rupee loans but also Indians employ their savings in sterling loans.

An equally significant approach to the composition of the public debt is its distribution over time as over space. Accordingly, the Indian public debt is classified as permanent and floating. The permanent debt has a comparatively long lease of life and consists of different loans with particular conditions attached to each. Borrowings of a purely temporary nature, such as issue of treasury bills, ways-and-means advances from the Reserve Bank, etc., are included within the floating debt. At present about 90 per cent of the rupee debt is permanent in nature. The whole of the sterling debt is generally permanent, except that very small amounts stand temporarily in a floating form. The English market is looked upon by the Government of India as a source of investment capital; it is not for meeting the day-to-day exigencies of finance.

Treasury bills occupy a very important place in the floating debt of India. The system of issuing treasury bills, which was first introduced in 1917, has now become a permanent feature of the Government's ways-and-means finance. These bills are repayable after two to twelve months, although three months treasury bills are most common and popular. They constitute the short-term borrowings of the Government. Week after week sums are borrowed with competitive tenders and week after week the maturing amounts are paid off. The balance represents the floating debt on this account. During the last five years the minimum amount outstanding of three months treasury bills has not fallen below Rs. 8 crores, while the maximum has reached as much as Rs. 85 crores. Thus a portion of the debt on this account is permanent in nature, though kept in a floating form. A large amount of the outstanding bills

is held in the Paper Currency Reserve as *ad hoc* securities. The treasury bills and the ways-and-means-advances from the Reserve Bank maintain parallelism between revenue and expenditure.

The other interest-bearing obligations of the Government of India constitute what is known as the unfunded debt, as it does not form any part of the funded or the consolidated debts. In other countries such debts are also called floating debt. There is a small sterling branch of the unfunded debt in England composed of the service funds overseas.

About 80 per cent of the Government of India's total interest-bearing obligations is covered by interest-bearing assets. The Indian public debt is mostly productive in nature. The greater portion of the amount raised has been employed in the construction and acquisition of Indian railways and in irrigation works and Posts and Telegraphs.

II

Origin and growth of public debt.—The Indian public debt has a history of a century and a half behind it. The nature of the obligation has had different phases along with the changes in the nature of British Administration in India. Originally the public debt constituted the liabilities of the East India Company arising out of various necessities for funds, commercial and administrative. The wars, which the East India Company carried on over land and waters in the East, gave occasion for such debts and the funds raised thereby were spent without any discrimination as between trade and administration. In fact, before 1814, the East India Company did not keep separate accounts of its double functions carried on for about half a century. In this period the several Mysore Wars, particularly the wars of Lord Wellesley, caused a heavy financial burden to the Administration and led to the accumulation of debt.

In 1813 the charter which renewed the East India Company's lease of life for a further period left it more of an

administrative corporation than a trading body, and consequently Indian territorial finance had to be separated from the Company's commercial finance. A very unscientific division was made due to want of clear records and the previous debt of the East India Company, whatever might have been the original cause of it, was placed upon the territorial branch, although the authorities were fully conscious of the inequity of the decision. It was assumed that henceforward "the administration of India was to be carried on separately as a *self-supporting unit*, regardless of the fact as to whether the administration would serve the interest of the people, the interest of the British nation, or even the Company's commercial interests." The life of this Charter witnessed some more hostilities. The Nepal War, the Mahratta War, the Burmese War, etc., augmented the debt of the East India Company.

In 1833 one more important decision was made. In extending the charter of the Company once more for twenty years, it was fully made into an administrative body; its commercial department was liquidated; the newly-formed Government of India was made to take over the assets and liabilities of the commercial department. Of the new liabilities imposed, one important item was the "home bond debt" of £3¼ millions about whose origin even the expert accountants could not find any trace. Another liability imposed was for £12 millions at 5 per cent on account of the East India Company's stock of £6 millions. The assets obtained on the other hand ultimately proved in 1874 to be insufficient to meet the liabilities for the stock. The balance of £4,579,416 was added to the permanent debt of India. The liabilities of 1833 were thus the original basis of the sterling debt of the Government. By a slow process of evolution the debt of the East India Company became the public debt of the Government of India.

The new Government of India being under the immediate direction of the British Government was made the sphere of influence of British foreign policy. British policy in India turned out very aggressive and forward. India became the field of a number of expensive wars in succession, for

example, the Afghan, Sind and Gwalior Wars, the two Sikh Wars, and the second Burmese War. The Indian Public debt continued to swell and by the time the Indian Mutiny broke out the amount nearly approached £60 millions. The Sepoy Mutiny added about £46 millions to the public debt of India. In 1862, when Indian finance was well under control, the public debt of India was over Rs. 96 crores. This was composed of over Rs. 63 crores registered in India and over £32 millions registered in England. The Mutiny compelled the Government to look to the English market for funds. The Indian public debt underwent a definite change in respect of policy and location.

Almost the whole of this debt was due to unproductive wars, an exception being made in 1855 when a loan was floated for public works. In the years which followed till the advent of the Great War, India did not witness so much of unproductive wars as previously. The Government of India changed their policy of aggression within the Indian borders. Beyond, military expeditions followed in quick succession, with which the Indian administration should have had little concern. Nevertheless, they cost the Government several crores of rupees. There were only two very expensive wars in India, the second Afghan War and the Burmese Wars. They cost the Government of India more than 25 crores of rupees.

Famines and fall in the rupee-sterling ratio of exchange were two other factors which caused unproductive loans. Nevertheless, the major portion of the public debt during the last quarter of the nineteenth century can be traced to the construction of public works such as railways and irrigation canals. By this time a movement, which had commenced among the English capitalists in India and England some forty years back, was taking gradual shape. In order to open up new channels of investment for British capital, which had been accumulating as a result of the Industrial Revolution in England, and to create new demands for British goods, a large expansion of public works in India with borrowed money was advocated. The Government of India once gave a hesitating response in 1855. When the

Mutiny impressed upon the authorities at Home and in India the urgency of developing communications, they took up the task of railway expansion and irrigation works in earnest. The requisite money was found by borrowing since 1867–68 on the acceptance of the principle by the Secretary of State in 1864. All expenditure on irrigation and railway development was charged to capital account. The Government at the same time incurred additional debt for the purchase of some existing railways and irrigation works from companies.

The whole of the productive debt shown in the accounts was not, however, caused *directly* by public works. On the recommendation of the Select Committee of 1878–79, the total public debt of India was to be classified as "Ordinary Debt" and "Public Works Debt," the two terms which have now assumed their respective names of "Unproductive" and "Productive" debts. All expenditure for the construction of productive public works was to be treated as borrowed money, whether the amount was actually borrowed or spent out of revenue surplus. If it was met from the revenue surplus, the ordinary debt of India was reduced in the accounts by a corresponding amount and the public works debt increased to the same extent, as if the surplus was used in paying off the unproductive debt and fresh debt was incurred for productive purposes, although actually no such debt was incurred and the public works were financed out of revenue surplus. These principles were given effect to in 1880–81. Everything was merely a matter of adjustment of accounts. The existing productive public debt of India does not give quite a true picture of its origin.

By the time India entered the War, the unproductive public debt of India was reduced to about Rs. 3 crores by this process of book entry. It would have been completely wiped off within a year or two. The War gave a new turn to the volume of Indian public debt. India made a war contribution of £100 millions and was faced with successive budgetary deficits (about 100 crores in 6 years). The necessary funds were raised by various devices. There was an additional expenditure of over Rs. 13 crores for

the construction of New Delhi. The unproductive public debt of India increased from Rs. 3 crores to nearly Rs. 258 crores in 1924, the first year of budgetary surplus since the War.

During this period the productive debts were advancing rapidly. Starting from Rs. 20 crores in 1875 the amount exceeded Rs. 100 crores in 1886, 200 crores in 1900, 300 crores in 1907, and 400 crores in 1914. Railways consumed the major portion of the funds. By 1875 the issue of railway *versus* irrigation was fought out decisively in favour of the former. Irrigation, which held the predominant attention before 1875, was only responsible for 22 per cent of the capital expenditure till 1900, 12 per cent till 1914, and 6 per cent since then. Due to the engagements in the War, capital expenditure on productive public works received considerable check. When the shock of it was over, the Government of India renewed their policy of heavy capital expenditure on railways. It was decided to spend 150 crores on railways in five years from 1922. The productive public debt of India increased by over 300 crores within a decade, due to the construction of railways, purchase of old lines, and assumption of the liabilities of some companies. The total Indian debt more than doubled after the War.

III

Financial aspects of public debt.—It is evident that the whole of the present productive public debt of India does not represent the amount of capital *borrowed* for productive purposes. A portion of the capital for the railway development could have been met out of the surplus revenue, while allowing the dead-weight debt to stand where it had been unless reduced by increased taxation, or unless Government were prepared to wait till the railway revenue could be in a position to reduce it. The policy adopted by the Government of India was not, however, unwise in a way, except that it gives a perverted view of the cause of Indian debt to-day. The Indian debt was only given a better

appearance and a more sound background to facilitate financial administration and create confidence among the investors.

The productive debt of India was not, however, productive in the sense that a businessman would understand it, till the advent of the present century. Before the year 1900 Indian railways yielded little profit to the State, the aggregate loss amounting to over £50 millions. The so-called productive debt was as much a burden upon the State finances as the unproductive debt. The original policy of classing that portion of the capital expenditure which was expected to yield at least 4 per cent net profit as productive proved for many years a myth. Secondly, railway development in certain parts of India, particularly on the frontiers, had no ostensible commercial purpose. They were strategic lines with small prospects of paying their way. They were definitely unproductive to a financier or investor. To a student of economics they are productive on account of their political and social services, and this is the fundamental measure of productivity.

Even when the railways were yielding profit they were not run on strictly commercial principles for the purpose of accounts. So also about other commercial activities. It was difficult to point out to what extent they were earning sufficiently to meet the cost of their capital. The desired reform in this direction was due to the financial genius of Sir Basil Blackett, who effected the separation of railway finance from general finance, commercialised the accounts of Posts and Telegraphs, and established Provincial Loan Funds so as to charge them with their due interest.

The problem of debt redemption is not very serious in India, as the productive debt represents the capital of commercial undertakings. So long as proper depreciation is allowed for, further arrangement for the recoupment of capital is unnecessary. The existing provision for the depreciation of capital invested in the railways is to make an annual contribution to a reserve, as opposed to a regular depreciation fund, sufficient to meet the cost of renewals as they fall due from time to time and not the original

cost of the wasting assets. In the strictly commercial sense the provision is unsatisfactory. If at a future date heavy replacement is called for, either general revenue will suffer or fresh loans will be required. The so-called productivity of the debt will prove to be a misnomer.

Provision for debt redemption.—A general and comprehensive provision for the redemption of the unproductive portion of the Indian public debt is only very recent, although, historically, the earliest experiment with sinking fund in India was made by Lord Wellesley in 1798, which was kept in operation for only a decade. Till 1924–25 India had no consolidated scheme for a sinking fund, and till to-day India has no statutory enactment as in England for regulation and administration of the sinking fund. Besides the measure adopted in 1878 for the reduction of unproductive debt, provisions for the avoidance of debt were specific. When some railway companies were purchased and liabilities to the English shareholders were undertaken, several Acts of Parliament imposed upon the State the duty and responsibility of constituting sinking funds from which railway annuities could be paid. This was, however, for the productive portion of the debt only. Specific provision was also made for a sinking fund to maintain the market price of the 5 per cent War Loan of 1917 and for annual payment of £500,000 in respect of India's war contribution. The plans for the avoidance of debt were thus haphazard and not based on any systematic policy. It was as late as 1924 that Sir Basil Blackett undertook a regular and comprehensive debt redemption scheme. According to this arrangement, the Government of India would regularly provide for, besides a fixed minimum of Rs. 4 crores, one-eightieth of the excess of the debt at the end of the expiring financial year over the amount on March 31, 1923, the sterling debt to be converted at 1*s.* 4*d.* per rupee. Certain classes of debt, such as treasury bills in the Paper Currency Reserve, etc., were omitted for obvious reasons in arriving at the balance. The scheme was operated as an experimental measure for five years till the end of 1929–30, since when it has been extended and

kept in force unchanged except that from 1930–31 the sterling debt was converted for calculation at the new parity of 1*s.* 6*d.* per rupee. It has been suspended from 1933–34 for financial reasons. When 60 per cent of the debt was attributed to the railways which were making no contribution to the general revenues, it would be imposing too heavy a burden on Indian finance. In his budget speech of 1935–36 the Finance Member promised for the future that "an increased provision for debt reduction ought to be a first charge on any contribution from the railways in the future." The present annual contribution to the Sinking Fund is Rs. 3 crores. During the period of its normal lease of life the Sinking Fund was enriched by occasional contributions. In the year 1925–26 the amount of customs duty on capital stores imported was added to it. It was a small sum of Rs. 20 lakhs only. Since 1926 the share of British India in the reparations payable by Germany has been applied to the reduction or avoidance of debt after payment of loss or damage due to enemy action in the War. This provision was subsequently repealed and no addition was made on this account with effect from 1930–31. Between 1926–27 and 1929–30, the amount of annual addition to the Sinking Fund from this source varied from Rs. 13 to Rs. 33 lakhs in round figures, while the total contribution from the general revenues was Rs. 55·79 crores between 1924–25 and 1934–35, *i.e.*, an average annual contribution of about 5 crores.

Purposes and limitations of the Sinking Fund.—The Sinking Fund is employed first to meet the provisions for amortisation attached to particular loans, and the balance is utilised to pay off the unproductive debt. So long as a large portion of the Indian debt is productive and so long as there exists a permanent programme for increasing capital expenditure, any attempt to wipe off the productive debt is unnecessary. This scheme of debt redemption has been of considerable utility in raising the existing credit and facilitating future borrowings.

Compulsory contribution for debt amortisation and uniformity of policy in the management of the debt through

a central fund are the two principal reasons why sinking funds are instituted. The old conception of the efficiency of a sinking fund in wiping off large debts by small contributions has been given up for good. It is only the compulsory payment which is significant. It makes for compulsory saving for what is to be paid, so that the future generation may not be overburdened with the expenditures of the past generations. So long, however, as the new debt incurred is more than the amount of annual contribution to the Sinking Fund, an increasing burden on the coming generation cannot be avoided. The Sinking Fund can equitably distribute the burden of debt over the future generations and make repayment less onerous, provided contributions are wisely made, if necessary, by fresh taxation. The annual contribution to the Indian Sinking Fund has been Rs. 5 crores on an average against an average addition of $7\frac{1}{2}$ crores to the total debt, but there has been little addition to the unproductive debt. In this respect the Sinking Fund in India has gone a long way towards its goal.

A consolidated fund has been established without any consolidated policy. Uniformity of policy is an essential desideratum of a Sinking Fund, for which National Debt Commissioners are appointed. They keep constant watch over conditions in the money market and ways of credit. The resources of the fund are brought under operation at the proper time to maintain credit while paying off the debt. When credit is low and the price of securities is below parity, the Commissioners come to the market to purchase them off. Repayment is effected at a profit. When, on the other hand, credit is high and the price of securities is at a premium, the resources of the fund help conversion so as to reduce the burden. The objective of the Sinking Fund in India is therefore yet to be realised.

There is no provision for the amortisation of the obligations accumulating through the channels of the P.O. Savings Banks and the Cash Certificates, although these amounts were taken into account in arriving at the annual contributions. Repayment of capital on these two accounts is usually met out of inflow. These obligations are allowed

to continue and gather strength by a constant process of change of hands. So long as there is no sudden loss of credit and a rush for withdrawal, a permanent provision for the ultimate repayment of these obligations is not quite so necessary; nor is it required when the Government need not look to the maintenance of their financial credit from day to day.

The problem of the payment of interest on P.O. Cash Certificates is different and peculiar to itself. The interest is not paid year by year but at the time of encashment and is termed "bonus." The bonus represents deferred interest and hence financially earlier years benefit at the expense of the later. Secondly, as the holders have got a right of encashment before maturity at a lower rate of interest after the first twelve months, which increases with the approach towards maturity, the inducement to the creditor to defer encashment is greater and there is no certainty about the actual amount to be repaid in a particular year. This uncertainty is further increased by the fact that even after maturity a certificate can be renewed for a further period. While the actual amount to be paid in a particular year is uncertain, the real liability of the year is concealed. The liabilities on account of the cash certificates were therefore accumulating. As the Indian budget is a cash budget, the provision made in the budget until 1930 had only covered the bonus actually expected each year and it was far short of the accruing liability. The real liability was allowed to accumulate concealed. In 1930 it was decided that the practice should no longer be allowed to continue and a new practice was introduced for providing each year for the actual accruing liability. The fund which has thus been created is called "The Post Office Cash Certificate Bonus Fund"; but it does not cover bonuses in arrears accrued before 1930.

IV

Special features and administration of the sterling debt.— The sterling debt of the Government of India is an interesting feature of the Indian public debt. It has involved

a good deal of controversy among writers, Indian and English. Its amount on March 31, 1935, was about £384 millions, which when converted into Indian units comes to about Rs. 512 crores. It is thus higher than the rupee portion of the Indian debt. This amount represents various loans raised in the English market by the Secretary of State, including the capital value of the debenture stocks of certain railway companies working in India, the liabilities in respect of which were assumed by the Secretary of State on termination of the contracts with them, £43·58 millions on account of the balance of the capital liabilities involved in the purchase of railways which are undergoing redemption by way of terminable railway annuities, and liability for the British Government's 5 per cent War Loan (1929–47) taken over by India, known as India's War Contribution, the balance of which at present stands at a figure of £16·72 millions. The whole amount is permanent in nature. Only sometimes a small amount rises in a floating form on account of India Bills outstanding.

The statutory position with regard to loans raised in England is peculiar to Indian constitutional development. One feature of the tutelage which Parliament exercises over the Government of India through the Secretary of State takes shape when the Secretary of State is required to obtain statutory sanction of Parliament for all loans raised in the English market. Since the first public loan in England in the year 1859 till 1923, whenever a loan was floated, separate and individual Parliamentary sanction had to be obtained by separate Acts. For all loans subsequent to 1923 no fresh Act has been enacted, the authority being always derived from the Act of 1923. The Dominions, on the other hand, are not required to obtain sanction of Parliament for individual loans floated in the English market. There is no statute for India analogous to the Colonial Stock Act of 1900 which places the Dominion securities in the category of trustee stocks. The separate Acts make up that defect and place Indian stocks in the position of trustee securities and raise their status in the investment market. The position of India in the London market is therefore very peculiar.

On this score Parliament takes frequent opportunity to criticise Indian financial policy and to burden Indian loans with terms and conditions which are not always to the interest of Indian finance. Any secrecy which a loan demands before being floated cannot be maintained. The Imperial Government does not guarantee the payment of either the principal or the interest; it will nevertheless exert its power of criticism and sometimes extract conditions favourable to the English capitalists, thus giving cause for strong criticism in India.

The sterling debt of the Government of India has a long history. When the Company was liquidated by the Act of 1833 and the Imperial Government of India was formed the new Government was burdened with the "bond debt" of the East India Company and the Company's capital stock at a double value. The bond debt of the Company commenced from 1698 and it fluctuated in amount throughout the Company's career. Originally the debt was solely due to the commercial function of the Company, but subsequently when the East India Company acquired Indian administration, a portion might have been caused by administrative necessities. The liquidation of the Company automatically transferred the burden of this bond debt to the Government of India. The amount was about £3½ millions. The capital stock of the Company was added to the sterling liabilities of the Government of India. The commercial assets of the Company which were handed over in compensation having proved insufficient, about £4½ millions were added in 1874 on this account. The first public loan was floated in the London money market in 1859 in order to meet the financial burden of suppressing the Indian Mutiny, which was too heavy to be met from Indian resources. Since then the London money market has been approached on more than one occasion. On the whole, the total volume of the debt was not very large till the advent of the War. It was nearly £120 millions at the commencement of the present century, and it went up to £175 millions during the War. It is during the post-war period that the amount has been

more than doubled. The increase is particularly large because of the liability assumed by the Secretary of State for certain Indian railways on termination of contracts with them.

During the last century the settled policy of the Government of India was to give outlet for English capital in India mostly through the guaranteed railway companies on their own account. The guarantee system of railway expansion was merely sowing the seeds of the future Indian public debt. The Government of India did not approach the Home market for general public works expenditure, except for the amounts raised in 1885–86 and 1886–87 on the recommendation of the Parliamentary Committee on Railways of 1884. A Sterling loan was considered advisable for discharging the then existing sterling debt carrying a higher rate of interest, or for purchasing specific railways, or on an exceptional occasion such as failure to raise funds in England by the sale of Bills by the Secretary of State due to the depressed condition of trade and fall in exchange. In the then undeveloped state of the Indian money market it could not be expected to supply more than 5 crores of rupees a year.

The unchallenged supremacy of England in trade and industry in the nineteenth century led to such large accumulations of capital in England that the demand for investment in India gained strength at the commencement of the present century. On the strength of the recommendation of the Mackay Committee, the Government of India adopted the policy of resorting to the London money market on an increasing scale. In the meantime the Indian money market gained strength. By the time the Mackay Committee's recommendations were given effect to, the London money market became dearer than at the commencement of the century. The post-war period did not improve the situation. Loans floated in London during the twenties had to be offered a higher yield than in India, the difference being sometimes to the extent of 1 per cent. The terms had to be highly attractive with definite assurance that the interest of the investors would be safeguarded under all

circumstances. Sterling debt became costlier to the Indian Government.

Between 1923 and 1927, the Government of India successfully avoided issue of any new sterling loan, although over £26 millions was spent outside India for capital outlay and £10 millions for reduction of sterling debt. The amount was financed by rupee funds. The policy was reversed in 1927 when there was disparity between the yields of stocks in London and Calcutta, leading to considerable transfer of money from India to London to take advantage of the higher yield there. The process continued till there was a final stabilisation of the rupee on a gold basis. The Finance Member had to go in for external borrowing. Since then the London money market has been systematically approached in the face of serious public criticism, although the Government have always asserted that in so far as money could not be raised from the investing public in India, recourse to sterling borrowing has to be had. But the extent of the capacity of the Indian market cannot be tested without risk to public credit. Its assessment therefore depends largely on the experience and discretion of the Finance Member.

The relative cheapness of sterling and rupee loans.—In 1923 the ratio between loans in India and England was 53·3 to 46·7. The 1935 ratio was 50·4 to 49·6. As the increase is mainly due to the liabilities assumed for the E.I.R. and the G.I.P.R. debenture stocks, it has been amply compensated by the acquisition of assets in India. The interest paid on ordinary debt in England is 3·7 per cent of the total amount of capital, against 4 per cent of the ordinary debt in India. It may appear at first sight that the interest on the foreign debt is lower than that on the rupee debt. Actually London is not the cheaper market of the two. Loans in London are offered a higher yield than rupee loans. Correspondingly there is a large increase in the capital value of the sterling debt where loans are issued at a high discount, and this was so in 1923, when the 7 per cent debt was converted into 3 per cent by offering double

the capital value to the investors. Between 1923 and 1935 the interest paid on ordinary debt in India came down from Rs. 20·11 crores to Rs. 19·54 crores, while in the same period the corresponding amount in England went up from Rs. 14·92 crores to Rs. 18·86 crores.

The position of India's English creditors in the London market is highly satisfactory. Almost the whole amount is productive and is backed by assets. The capital is raised by a representative of the British Cabinet in the name of the Government administered by a representative of the Crown. The financial position of India is in no way worse than that of any other Government. There is in particular a regular provision for the redemption of debt. India has never been a defaulter, nor even unpunctual, like some other Governments borrowing in the London market. English capitalists and industrialists have every reason to look upon Indian loans with favour not merely for their attractive terms but also for the reason that the amount of purchasing power pooled is allowed to recirculate in the country through the purchase of English materials for Indian railways. There cannot, therefore, be any foundation for the excuse that India's credit in the London money market is low. In fact, the market yields of the Indian stocks in the London exchange are lower than the yields of many Colonial and Dominion Government securities. Indian stocks range next to the British Funds, showing how the London investors actually assess the credit of Indian stocks. The allegation that the credit of India among the foreign investors is low is merely a myth.

V

The rupee debt and its characteristics.—The rupee portion of the public debt was administered by the Controller of the Currency in a separate department known as the Central Public Debt Office. The management of the Central Public Debt Office is now in the hands of the Reserve Bank of India. The management is regulated by an agreement with

the Bank. The sterling portion of the debt is managed by the Banks of England and Ireland. There is no fixed rule to guide the actual policy of administration. It is influenced by various circumstances, the nature and condition of maturing debts, the expediency and urgency of the Government finances, and the condition of the money market.

For over a decade the Government of India have been consistently following a policy of increasing the proportion of the unfunded debt in India to the funded debt. Receipts in the Savings Banks and subscriptions to the Cash Certificates, etc., have increased considerably. Particular attention has been paid to making the Cash Certificates more popular since 1923 by offer of high bonus. The offers of 1923, for example, were so modelled as to yield 6 per cent compound interest, although the present yield is much lower (3 per cent). In effect, between 1923 and 1935 the total volume of unfunded debt coming under the term "Other Obligations" increased from over Rs. 65 crores to nearly Rs. 235 crores, the increase of its ratio to the funded debt in India being from 16 per cent to over 48 per cent. The capital value of Indian obligation is thus increasing on the more burdensome items.

Cash certificates have some relieving features. Unlike the regular annual rupee loans they are always "on tap." The funds mainly come out of small investors and therefore do not affect the capital market very much. When a certificate is cashed the whole portion of the money withdrawn does not return to finance consumption goods; a considerable amount goes to add to the investment capital of the country and is used for re-investment in house property, business or some kind of marketable security. All the time a class of small investors is being created in the process. The Cash Certificate has therefore been adopted as one among the instruments of encouraging the investment habit of the people. As a security it combines in itself features belonging to savings banks deposits, in particular the facility for encashment at any time and protection against any risk of depreciation in value, together with some of the characteristics of an investment. It may be

regarded as an ideal security for the very small investor, enabling him to cross the bridge dividing a depositor in a savings bank from a holder of marketable investment securities. Its capital value is not subject to depreciation. Complaints have often been made that the certificate competes with the joint-stock banks and checks the growth of bank deposits. Such an allegation seems to have no foundation. The Cash certificate may on the other hand help the growth of deposits by encouraging accumulation of funds from neglected corners. It is, however, inelastic in respect of the rate of interest and it maintains little relation with the market rate of interest. Although the rate has now been very much reduced, the burden of the debt on this account is still very high. So also about the burden of the Provident Funds.

A large amount of unfunded debt is highly risky from the financial point of view. Experience during the war showed that a sudden run on the savings banks by depositors can expose the Government to insurmountable difficulties. Cash certificates are not safer either. In spite of their fixed lease of life the holders are at liberty to withdraw their sums at any time and at compromise rates of interest after the expiry of the first year. The only attraction of these sources of funds to the Government is that during the normal period amounts pour into the Government coffers without disturbing the money market and without exposing themselves to much public criticism. They are all the more attractive when current demands for repayment are met out of funds flowing in, so that in a normal period the problem of redemption is very easy and simple. But the obligation cannot be ultimately avoided, and a sudden run may expose the Government to utter discredit. For several months past the inflow of funds by sale of cash certificates has been known to be less than the outflow and the balance is being either paid out of savings bank deposits or revenue.

The volume of debt on treasury bills varies from time to time in accordance with the ways and means requirements and financial policies of the Government. In fact, issue of treasury bills was stopped in 1924 (Jan. 27) and

reintroduced in 1927 (Aug. 9). These bills have certain important economic features. The discount represents prepaid interest as opposed to the bonus on cash certificates which is paid at the time of encashment. The interest is therefore debited to the year in which bills are issued and the later year may benefit at the expense of the earlier, although the chances for the maldistribution of the burden are not serious when the currency of the bills is short. As the treasury bills are secured by competitive tenders, the rate of discount follows the market rate of interest for short-term loans instead of the market rate following the bill rate as determined by the Government. But the market rate itself is not an independent function of other factors. The inflow and outflow of funds in the market through the discharge and issue of treasury bills influence the supply and demand of short-term money in the market, and regulate the market rate itself. The treasury bill is thus an important instrument for controlling the seasonal supply of money in the market, the market rate of interest, and also for checking the seasonal fluctuations of the prices of the giltedge. It improves the financial facilities of the Indian money market and renders a safe avenue for the employment of the short-term funds of the banks and business people.

Reduction of interest charges.—During the last decade the burden of interest on Indian revenue has decreased steadily. The net interest charge, after deducting the amount charged to railways, irrigation, Posts and Telegraph, Provincial Loan Fund, and other heads, has come down from Rs. 14·90 crores to Rs. 10·28 crores between 1924–25 and 1934–35. This is not so much due to actual reduction of the rates of interest on the debt as to increasing charge on Indian railways, which has gone up from Rs. 21·23 crores to Rs. 30·81 in the same period. The gross interest actually increased from Rs. 37·56 crores to Rs. 44·57 crores by 1931–32. In the revised estimate for 1934–35, the amount is lower and is Rs. 39·77 crores. The benefits of the savings resulting from conversion operations and lower rates on new borrowings are just being

felt. There will be further alleviation of the burden of debt at the present state of credit and the low market rate of interest, although the tenacity of railway depression may cause disappointment.

Besides the actual rates of interest paid, there is a secret burden of interest. Most of the loans have been issued at discount with low rates of interest so framed as to give the market rate to the investor. This system, although not a peculiar feature of Indian loans, either places a secret burden of interest on the annual revenues or adds to the capital of the debt. Of the loans issued in India the present practice is said to be to distribute the amount of discount over the life of the loan and charge the annual revenue, while for all sterling loans the practice has been to charge the year of issue for the whole amount of the discount on account of the loan or loans issued in that year. In the latter case the present generation is penalised in favour of posterity. The system in India stands in favourable contrast to that in many other countries where the capital of the national debt is swelled for the amount of the discount, placing accumulated burden on the future generation. To add any portion of the interest to the capital of the debt is to pay a compound rate of interest to some extent. Relief in the current taxation is rather apparent. An apparently fictitious rate of interest far from the market rate on investment capital places both the State and the investor in a state of uncertainty. A further rise in the market rate depresses the price of the securities extremely low. Conversely, a fall in the market rate must be abnormal to allow the State to undertake with confidence any conversion operation. Sometimes, however, issue at discount is considered advisable. When a security is above parity in the market and a new security of its kind is not wanted to be issued at premium, a new loan at the next lower rate of interest may require to be issued at discount without prejudicing the price of the old securities and ruining the interest of the investors and State credit.

VI

Consequences of public debt.—The burden of the public debt of India is not great. The common way of arriving at it is to find out the average amount per head. On the basis of the population in 1931 in British India the *per capita* amount comes up to Rs. 45½ when the total obligation is Rs. 12,35·74 crores. This is much less than half the national dividend per head of Indian population, on the basis of Professor Findlay Shirras's calculation (Rs. 116) for 1922. Taking into account the increase in the number of population in the meantime, the advent of the depression, and consequent fall in prices, the amount of debt per head will be about half the income. Such a presentation of the burden of debt on Indian population has, however, little value when about 1,000 crores is backed by interest-bearing assets, when the whole population is not taxed, and when there are many who are either females, or young, or old, or unemployed. The total amount of interest on Indian debt after reduction of the amounts charged to various departments is about Rs. 10 crores (Rs. 9·29 crores in 1933–34) and is about 12 per cent of the total net revenue or net expenditure charged to revenue. This compares very favourably with the defence burden which eats up more than half the tax revenue.

Public debt has various economic consequences upon production and distribution of wealth which vary in accordance with the purpose of the debt, sources of the fund, and the place of it in the financial and economic structure of the nation. That portion of the debt which represents the amount of capital of the nation adds to its own wealth and welfare, the economic and social benefits of which cannot be exaggerated. The public debt of India has amply justified its purpose. It has served the cause of efficient administration and armed the State with a standing machinery to cope with famine. Politically and economically India has progressed a good deal towards unification. External and internal trade has been increased. New avenues of agri-

cultural, mineral and industrial production have been opened to the public. Wider sources of direct employment have been created.

Recent views on public debt.—Public debt for the economic and social uplift of India has been advocated along with the desire for expansion of public works in India since Indian trade was opened to the British public. Colonel Arthur Cotton was its staunchest supporter and he found in the traders and merchants of Manchester, Liverpool and Bristol a large following. The contemporary pamphlets which constituted the economic literature of the time embodied this current of thought. This view was officially accepted by Sir Charles Wood in a dispatch and Lord Dalhousie assented, since when the Government of India have not turned away from this source of capital. With the commencement of the present century new economic thoughts were gaining ground in India. Following the arguments of Major Wingate in the middle of the last century, who was a great critic of the British public debt policy, some Indian writers gave a different interpretation of Indian public debt and read in it the ties of Indian bondage. Indian political agitators were brought up in this concept. It took a very extreme form with the growth of radicalism in the political consciousness of India, resulting in the demand for repudiation of a portion of Indian debt or for reparation from the British Government for a share of it. In the haze of controversy which ensued on the subject, the political, economic and financial status of India was forgotten, the earliest purpose of the debt was given great prominence, the later object of it was ignored, and the present and future prospect of Indian public credit was put in jeopardy. A wholesale nation-wide bias was created against the purpose and utility of public borrowing for economic services. Recently a different lead has been given by trained economists. Following the arguments which are now swaying the West, economic thinkers are advocating expansion of public works in India to be financed by public borrowing by the State. The arguments for reflation have found wide favour in India as a remedy for

the present economic depression and consequent unemployment. It is doubtful whether a remedy of the type which might have favourable consequence in some of the small industrial countries of the West can take India nearer to her objective. Public works create demand for industrial commodities and industries like engineering, iron and steel, coal, building materials, etc., and the benefit gradually permeates the whole economic structure of the country. By thus giving an artificial stimulus to the demand for industrial produce, an industrial country like Great Britain may be led out of the quagmire of economic depression and unemployment. India is a vast agricultural country without much economic coherence. To infuse circulating medium in the land by public works is a work of too vast dimensions to be adopted. Drops of money here and there will not cure so widespread a disease. Public works in India will only create demand for commodities to the great benefit of foreign industry, and for labour to the benefit of urban population. The best sort of public works in India to serve the purpose might have been a network of road construction in the Indian villages far and wide. The money would be mostly spent on labour and in villages. The new purchasing power would then create demand for agricultural commodities. Still, as a quick remedy for depression the work cannot be advocated with confidence. India, which can digest with equanimity hundreds of crores' worth of gold without disturbance to the price level, has too rigid an economic structure to respond to the remedy advocated. On this score the Government of India should not pile up uneconomic public debt.

Nevertheless, the Government of India have not given up their old policy of financing capital expenditure out of public loans, not in any hope of finding out a ready remedy for depression but of slowly working for the financial prosperity and general economic welfare of the country. Their policy in recent years has been to spend money freely on capital expenditure and to raise a large portion of it by public loans, keeping at the same time the total amount under effective control without overstraining the market

and jeopardising the credit. The two guiding principles are to undertake those objects of capital expenditure which are economically sound and productive and to avoid programmes on a disproportionately large scale, making the posterity pay.

Sterling loan *versus* rupee loan.—The greatest part of the controversy on Indian public debt has been on the position of foreign capital in the national debt of India. Extreme views still prevail in the country. The problem came up for rational consideration before the External Capital Committee and the verdict has been in favour of external capital for the economic development of India so long as indigenous capital is not forthcoming. The argument of the economist is nothing much different. Foreign capital without foreign political control is desirable for India, although the latest constitutional document of India gives statutory permanence to that control in the name of safeguarding the interest of the foreign capital in India.

In the choice between sterling loan and rupee loan, the problem is threefold. The Government are to assess properly the elasticity of supply of capital in the Indian market in proportion to the rates of return and other advantages offered. They cannot afford to impose a serious burden on the taxpayer by offering a high yield in order to keep public loans restricted to the home market. Nor should they seriously injure the claim of Indian trade and capital in the home market. External borrowing under such conditions is a mark of financial wisdom provided the sacrifice in money and autonomy is not very great.

The sterling debt of India is associated with the problem of Indian Home Charges, Balance of Trade and rates of exchange. The amount of interest paid to India's overseas creditors forms a large part of the Home Charges. Loans floated exert a favourable influence over Indian exchange, while the payment of interest works in the contrary way. It has often been contended by the critics of the Government that they have sometimes purposely manipulated Indian exchange by floating unnecessary sterling loans.

In normal course India requires to maintain a large favourable balance of visible trade to meet the burden of her foreign obligations and to prevent the exchange from falling much below parity. During the last decade India's favourable balance of trade in merchandise has come down from nearly 147 crores to 21 crores. In these days of excessive economic nationalism there is very small hope of India regaining her former position. To-day the position has been maintained by an abnormal gold export. But very soon it may be greatly burdensome for India to meet her foreign obligations, unless they are met out of new loans, a very dangerous practice in national and international finance. The United States of America has been the latest victim of a similar policy followed by many Central European countries. India should therefore replace her foreign obligations by rupee debt as far as possible. Otherwise, Indian trade, currency, exchange, and finance will be in a muddle.

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